DOCKET

SUPREME COURT
OF THE UNITED STATES

No. 11-139
Title: United States, Petitioner
v.
Home Concrete & Supply, LLC, et al.
Docketed: August 3, 2011
Linked with 10A1259
Lower Ct: United States Court of Appeals for the Fourth Circuit
Case Nos.: (09-2353)
Decision Date: February 7, 2011
Rehearing Denied: April 5, 2011
Questions Presented

~~Date~~~	~~~~~~~Proceedings and Orders~~~~~~~~~~~~~~~~~~~~
Jun 22 2011	Application (10A1259) to extend the time to file a petition for a writ of certiorari from July 4, 2011 to August 3, 2011, submitted to The Chief Justice.
Jun 22 2011	Application (10A1259) granted by The Chief Justice extending the time to file until August 3, 2011.
Aug 3 2011	Petition for a writ of certiorari filed. (Response due September 2, 2011)
Aug 26 2011	Brief of respondents Home Concrete & Supply, LLC, et al. in opposition filed.
Sep 2 2011	Brief amicus curiae of Bausch & Lomb Incorporated filed.
Sep 7 2011	DISTRIBUTED for Conference of September 26, 2011.
Sep 20 2011	Reply of petitioner United States filed. (Distributed)
Sep 27 2011	Petition GRANTED.
Nov 1 2011	The time to file the joint appendix and petitioner's brief on the merits is extended to and including November 15, 2011.
Nov 15 2011	Joint appendix filed.
Nov 15 2011	Brief of petitioner United States filed.
Nov 18 2011	CIRCULATED.
Nov 22 2011	Consent to the filing of amicus curiae briefs, in support of either party or of neither party, received from counsel for the respondents.
Nov 23 2011	Consent for the filing of amicus curiae briefs in support of either party or neither party received from counsel for petitioner.
Nov 25 2011	Record received from U.S.C.A. Fourth Circuit.
Nov 25 2011	Record from U.S.D.C. for Eastern District of North Carolina (Southern Division) is electronic.
Dec 14 2011	SET FOR ARGUMENT ON Tuesday, January 17, 2012.
Dec 15 2011	Brief of respondents Home Concrete & Supply, LLC, et al. filed. (Distributed)

Dec 22 2011	Brief amicus curiae of National Association of Home Builders filed. (Distributed)
Dec 22 2011	Brief amici curiae of National Federation of Independent Business Small Business Legal Center, et al. filed. (Distributed)
Dec 22 2011	Brief amicus curiae of American College of Tax Counsel filed. (Distributed)
Dec 22 2011	Brief amicus curiae of Grapevine Imports, Ltd. filed. (Distributed)
Dec 22 2011	Brief amici curiae of UTAM, Ltd. and DSDBL, Ltd. filed. (Distributed)
Dec 22 2011	Brief amicus curiae of Bausch & Lomb Incorporated filed. (Distributed)
Dec 22 2011	Brief amici curiae of Daniel S. Burks and Reynolds Properties, L.P. filed. (Distributed)
Dec 22 2011	Brief amicus curiae of Government of the United States Virgin Islands filed. (Distributed)
Dec 22 2011	Brief amicus curiae of Professor Kristin E. Hickman filed. (Distributed)
Jan 10 2012	Reply of petitioner United States filed. (Distributed)
Jan 17 2012	Argued. For petitioner: Malcolm L. Stewart, Deputy Solicitor General, Department of Justice, Washington, D. C. For respondents: Gregory G. Garre, Washington, D. C.
Apr 25 2012	Adjudged to be AFFIRMED. Breyer, J., delivered the opinion of the Court, except as to Part IV-C. Roberts, C. J., and Thomas and Alito, JJ., joined that opinion in full, and Scalia, J., joined except for Part IV-C. Scalia, J. filed an opinion concurring in part and concurring in the judgment. Kennedy, J., filed a dissenting opinion, in which Ginsburg, Sotomayor, and Kagan, JJ., joined.

PETITION FOR WRIT OF CERTIORARI

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

DONALD B. VERRILLI, JR.
Solicitor General
Counsel of Record
JOHN A. DICICCO
Principal Deputy Assistant Attorney General
MALCOLM L. STEWART
Deputy Solicitor General
JEFFREY B. WALL
Assistant to the Solicitor General
MICHAEL J. HAUNGS
JOAN I. OPPENHEIMER
Attorneys
Department of Justice
Washington, D.C. 20530-0001
SupremeCtBriefs@usdoj.gov
(202) 514-2217

QUESTIONS PRESENTED

As a general matter, the Internal Revenue Service (IRS) has three years to assess additional tax if the agency believes that the taxpayer's return has understated the amount of tax owed. 26 U.S.C. 6501(a). That period is extended to six years, however, if the taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the [taxpayer's] return." 26 U.S.C. 6501(e)(1)(A). The questions presented are as follows:

1. Whether an understatement of gross income attributable to an overstatement of basis in sold property is an "omi[ssion] from gross income" that can trigger the extended six-year assessment period.

2. Whether a final regulation promulgated by the Department of the Treasury, which reflects the IRS's view that an understatement of gross income attributable to an overstatement of basis can trigger the extended six-year assessment period, is entitled to judicial deference.

PARTIES TO THE PROCEEDINGS

Petitioner is the United States of America.

Respondents are Home Concrete & Supply, LLC; Robert L. Pierce; Susanne D. Pierce; Stephen R. Chandler; Rebecca R. Chandler; and Home Oil and Coal Company, Inc.

TABLE OF CONTENTS

Page

Opinions below 1
Jurisdiction 1
Statutory and regulatory provisions involved 2
Statement 2
Reasons for granting the petition 7
Conclusion 8
Appendix A – Court of appeals opinion (Feb. 7, 2011) ... 1a
Appendix B – Court of appeals rehearing order (Apr. 5, 2011) 22a
Appendix C – District court order (Nov. 21, 2008) 23a
Appendix D – Statutory and regulatory provisions 47a

TABLE OF AUTHORITIES

Cases:

Beard v. *CIR*, 633 F.3d 616 (7th Cir. 2011), petition for cert. pending, No. 10-1553 (filed June 23, 2011) 3, 4, 7
Kornman & Assocs., Inc. v. *United States*, 527 F.3d 443 (5th Cir. 2008) 3
Jade Trading, LLC v. *United States*, 80 Fed. Cl. 11 (2007), aff'd in relevant part, 598 F.3d 1372 (Fed. Cir. 2010) 4
The Colony, Inc. v. *CIR*, 357 U.S. 28 (1958) 6

Statutes and regulation:

Internal Revenue Code (26 U.S.C.):
26 U.S.C. 61(a)(3) 2
26 U.S.C. 722 3
26 U.S.C. 723 3
26 U.S.C. 752 ..... 3, 4

Statutes and regulation—Continued: Page

26 U.S.C. 1011(a) 2
26 U.S.C. 1012 2
26 U.S.C. 6501(a) 2, 5, 6
26 U.S.C. 6501(e)(1)(A) 2, 5, 6, 7
26 U.S.C. 7609(e)(2) 6
26 C.F.R. 301.7701-3(b)(1)(i) 4

Miscellaneous:

IRS Notice 2000-44, 2000-36 I.R.B. 255 4

In the Supreme Court of the United States

No. 11-139

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

The Solicitor General, on behalf of the United States of America, respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fourth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-21a) is reported at 634 F.3d 249. The opinion of the district court (App., *infra*, 23a-46a) is reported at 599 F. Supp. 2d 678.

JURISDICTION

The judgment of the court of appeals was entered on February 7, 2011. A petition for rehearing was denied on April 5, 2011 (App., *infra*, 22a). On June 22, 2011, the Chief Justice extended the time within which to file a petition for a writ of certiorari to and including August

3, 2011. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

The relevant statutory and regulatory provisions are reproduced in the appendix to this petition. App., *infra*, 47a-72a.

STATEMENT

1. As a general matter, the Internal Revenue Service (IRS) has three years to assess additional tax if the agency believes that the taxpayer's return has understated the amount of tax owed. 26 U.S.C. 6501(a). That period is extended to six years, however, if the taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the [taxpayer's] return." 26 U.S.C. 6501(e)(1)(A). The question presented in this case is whether that six-year assessment period applies to a tax-avoidance scheme that operated by overstating a taxpayer's basis in property.

a. When a taxpayer sells property, any "[g]ain[]" that he realizes from the sale contributes to his "gross income." 26 U.S.C. 61(a)(3). The taxpayer's gain, however, is not the sale price of his property. Rather, it is the sale price minus the taxpayer's capital stake in the sold asset, which is generally the amount paid to obtain the property, as adjusted by various other factors. 26 U.S.C. 1012. For tax purposes, that capital stake is commonly referred to as the taxpayer's "basis" in property. 26 U.S.C. 1011(a). Because the taxable income from a property sale is generally determined by subtracting the taxpayer's basis from the property's sale price, an overstatement of basis will typically decrease

the amount of the taxpayer's gain (and thus the amount of federal income-tax liability) that is attributable to the sale.

This case involves a particular kind of tax shelter, known as a Son-of-BOSS (Bond and Option Sales Strategy) transaction. In a Son-of-BOSS transaction, a taxpayer uses some mechanism, often a short sale, to artificially increase his basis in an asset before the asset is sold. A short sale is a sale of a security that the seller does not own or has not contracted for at the time of the sale. To close the short sale, the seller is obligated to purchase and deliver the security at some point in the future, often by using the proceeds from the short sale itself. App., *infra*, 3a n.1. Typically in a Son-of-BOSS transaction, a taxpayer enters into a short sale and transfers the proceeds as a capital contribution to a partnership. The partnership then closes the short sale by purchasing and delivering the relevant security on the open market. See *Beard* v. *CIR*, 633 F.3d 616, 617-618 (7th Cir. 2011), petition for cert. pending, No. 10-1553 (filed June 23, 2011).

When the taxpayer and partnership file their tax returns for the year in which a transaction of the kind described above occurs, they are required under 26 U.S.C. 722, 723, and 752 to report their taxable bases in the partnership. The taxpayer's basis in the partnership is called an "outside basis," while the partnership's basis in its own assets is called an "inside basis." See *Kornman & Assocs., Inc.* v. *United States*, 527 F.3d 443, 456 n.12 (5th Cir. 2008). In a Son-of-BOSS transaction, when computing both "outside" and "inside" basis, the taxpayer and the partnership include the short-sale proceeds contributed to the partnership, without decreasing that amount by the corresponding obligation (*i.e.*, to

close the short sale by purchasing and delivering the relevant security) that the partnership has assumed. As a result, the taxpayer either generates a large paper loss that can be used to offset capital gains on other unrelated investments, or turns what would otherwise have been a sizeable capital gain into a smaller taxable gain or even a capital loss.[1] See *Beard*, 633 F.3d at 618.

b. In this case, respondents Stephen R. Chandler and Robert L. Pierce were the sole shareholders of respondent Home Oil and Coal Company, Inc. (Home Oil), which they planned to sell. In order to minimize their tax liability, they formed a pass-through entity in April 1999 called Home Concrete & Supply, LLC (Home Concrete).[2] In May 1999, the taxpayers participated in a short sale of United States Treasury Notes, receiving cash proceeds of more than $7.4 million. They then transferred that entire amount, along with the obligation to close out the short position, to Home Concrete.

---

[1] In 2000, the IRS issued a notice informing taxpayers that Son-of-BOSS transactions were invalid under the tax laws. See Notice 2000-44, 2000-36 I.R.B. 255 (describing arrangements that unlawfully "purport to give taxpayers artificially high basis in partnership interests"). In the wake of that notice, courts largely have invalidated Son-of-BOSS transactions as lacking in economic substance. See, *e.g.*, *Jade Trading, LLC* v. *United States*, 80 Fed. Cl. 11, 45-46 (2007), aff'd in relevant part, 598 F.3d 1372, 1376-1377 (Fed. Cir. 2010). In 2004, the IRS offered a settlement to approximately 1200 taxpayers. Many taxpayers who had engaged in Son-of-BOSS transactions, however, either did not qualify, chose not to participate in the settlement, or had not yet been identified. See *Beard*, 633 F.3d at 618.

[2] Home Concrete was a limited liability corporation, which for present tax purposes is treated in the same manner as a partnership. See 26 U.S.C. 752; 26 C.F.R. 301.7701-3(b)(1)(i). This brief therefore refers to the ownership interests in Home Concrete as partnership interests.

The following day, Home Concrete closed the short sale by purchasing and delivering Treasury Notes for slightly less than $7.4 million. The taxpayers later executed a series of transactions through which they transferred virtually all of Home Oil's assets to Home Concrete, and they then sold Home Concrete for approximately $10.6 million. App., *infra*, 2a-3a.

In April 2000, Chandler and his wife, respondent Rebecca R. Chandler; Pierce and his wife, respondent Susanne D. Pierce; and Home Concrete filed their federal income-tax returns for 1999. In computing both their inside and outside bases, the taxpayers and Home Concrete included the amount of the short-sale proceeds (more than $7.4 million) that had been contributed to Home Concrete, without reducing that amount to reflect Home Concrete's offsetting obligation to close the short position. As a result, Home Concrete reported only a modest gain of $69,125 on the $10.6 million sale of its assets. App., *infra*, 4a.

2. In September 2006, the IRS issued a Final Partnership Administrative Adjustment (FPAA), decreasing to zero the taxpayers' outside bases in Home Concrete and thereby substantially increasing their taxable income for 1999. Respondents challenged the FPAA, arguing that it was barred because it was issued after the expiration of the three-year assessment period provided by 26 U.S.C. 6501(a). The government contended that the FPAA was governed instead by the extended six-year assessment period in 26 U.S.C. 6501(e)(1)(A), which applies when a taxpayer "omits from gross income an amount properly includible therein which is in excess

of 25 percent of the amount of gross income stated in the return."[3]

The district court granted partial summary judgment to the United States. App., *infra*, 23a-46a. It ruled that "where a taxpayer overstates basis and, as a result, leaves an amount out of gross income, the taxpayer 'omits from gross income an amount properly includible therein' for purposes of [Section] 6501(e)(1)(A)." *Id.* at 39a. The court therefore concluded that the six-year period in Section 6501(e)(1)(A), and not the three-year period in Section 6501(a), applied to the IRS's assessment. *Ibid.* The court rejected respondents' argument that this Court's decision in *The Colony, Inc.* v. *CIR*, 357 U.S. 28 (1958) (*Colony*), required a different result. The court explained that *Colony* had involved an earlier provision of the Internal Revenue Code, and that subsequent statutory amendments make clear that *Colony*'s holding does not apply to the current Section 6501(e)(1)(A). App., *infra*, 32a-38a.

3. The court of appeals reversed. App., *infra*, 1a-21a. The court concluded that "*Colony* forecloses the argument that Home Concrete's overstated basis in its reporting of the short sale proceeds resulted in an omission from its reported gross income." *Id.* at 11a. The court declined to apply a regulation promulgated in temporary form by the IRS in September 2009, which became final while the appeal was pending, and which con-

---

[3] Although the FPAA was issued in September 2006, more than six years after the taxpayers filed their returns in April 2000, the assessment period was suspended for approximately five months (between December 2003 and May 2004) due to a third-party recordkeeper's tardy compliance with an IRS summons. See C.A. App. 326 n.5; see also 26 U.S.C. 7609(e)(2). Respondents do not dispute that if the six-year assessment period applies, the FPAA in this case was timely.

strues the phrase "omits from gross income" to encompass situations in which a taxpayer understates his income by overstating his basis in property. *Id.* at 16a. The court held that the regulation was inapplicable by its terms, and that this Court's decision in *Colony* had found the relevant statutory language unambiguous and thus precluded any contrary agency interpretation. *Id.* at 12a-16a.

REASONS FOR GRANTING THE PETITION

This case presents the question whether an understatement of gross income attributable to an overstatement of basis in sold property is an "omi[ssion] from gross income" that can trigger the six-year assessment period in 26 U.S.C. 6501(e)(1)(A). That question is presented in a petition for a writ of certiorari currently pending before the Court. See *Beard* v. *CIR*, 633 F.3d 616 (7th Cir. 2011), petition for cert. pending, No. 10-1553 (filed June 23, 2011). The government agrees with the petitioners in *Beard* that this Court should grant review in that case in order to resolve a conflict among the circuits. See Gov't Br., *Beard*, *supra*, at 19-20 (filed July 27, 2011).

Beard is the earlier-filed petition, and the government is not aware of any reason why this case would present a more suitable opportunity than *Beard* for resolving the circuit conflict. If the Court grants the petition in *Beard* and concludes that an overstatement of basis in sold property does trigger the extended six-year assessment period, then the assessments at issue in this case were timely and the court of appeals erred in holding otherwise. Accordingly, the Court should hold this petition pending the disposition of *Beard*, including any

subsequent proceedings on the merits, and then dispose of the petition as appropriate in light of those decisions.

CONCLUSION

The petition for a writ of certiorari should be held pending the Court's final disposition of *Beard* v. *CIR*, petition for cert. pending, No. 10-1553 (filed June 23, 2011), and then disposed of as appropriate.

Respectfully submitted.

DONALD B. VERRILLI, JR.
Solicitor General
JOHN A. DICICCO
Principal Deputy Assistant Attorney General
MALCOLM L. STEWART
Deputy Solicitor General
JEFFREY B. WALL
Assistant to the Solicitor General
MICHAEL J. HAUNGS
JOAN I. OPPENHEIMER
Attorneys

AUGUST 2011

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 09-2353

HOME CONCRETE & SUPPLY, LLC; ROBERT L. PIERCE; STEPHEN R. CHANDLER; REBECCA R. CHANDLER; HOME OIL AND COAL COMPANY, INCORPORATED; SUSANNE D. PIERCE,
PLAINTIFFS-APPELLANTS

v.

UNITED STATES OF AMERICA, DEFENDANT-APPELLEE

BAUSCH & LOMB, INC., AMICUS SUPPORTING APPELLANTS

Argued: Oct. 27, 2010
Decided: Feb. 7, 2011

OPINION

Before: WILKINSON, GREGORY, and WYNN, Circuit Judges.

WYNN, Circuit Judge:

In *Colony, Inc. v. Commissioner of Internal Revenue*, the United States Supreme Court held that an

overstatement of basis in assets resulting in an understatement of reported gross income does not constitute an "omission" from gross income for purposes of extending the general three-year statute of limitations for tax assessments. 357 U.S. 28, 78 S. Ct. 1033, 2 L. Ed. 2d 1119 (1958). Because *Colony* squarely applies to this case, and because we will not defer to Treasury Regulation § 301.6501(e)-1(e), which was promulgated during this litigation and, by its own terms, does not apply to the tax year at issue, we reverse and hold that the tax assessments at issue here were untimely.

I.

In 1999, plaintiffs Stephen R. Chandler and Robert L. Pierce were the sole shareholders of plaintiff Home Oil and Coal Company, Incorporated ("Home Oil"). Mr. Pierce contemplated selling his interest in Home Oil and sought professional financial planning advice in anticipation of the transaction. This financial advice, rendered by several financial planning firms, included proposals to minimize the tax liability generated by Mr. Pierce's sale of his interest in Home Oil. The ensuing transactions form the grounds of this dispute.

Plaintiff Home Concrete & Supply, LLC ("Home Concrete"), a pass-through entity for tax purposes, was formed on April 15, 1999. Its partners were Mr. Chandler, Mr. Pierce, Home Oil, and two trusts established for the benefit of Mr. Pierce's children (collectively "the taxpayers").

On May 13, 1999, each of the taxpayers initiated short sales[1] of United States Treasury Bonds. In the

[1] A "short sale" is a "sale of a security that the seller does not own or has not contracted for at the time of sale, and that the seller must bor-

aggregate, the taxpayers received $7,472,405 in short sale proceeds. Four days later, the taxpayers transferred the short sale proceeds and margin cash to Home Concrete as capital contributions. By transferring the short sale proceeds to Home Concrete as capital contributions, the taxpayers created "outside basis" equal to the amount of the proceeds contributed.[2] The next day, May 18, 1999, Home Concrete closed the short sales by purchasing and returning essentially identical Treasury Bonds on the open market at an aggregate purchase price of $7,359,043.

On June 11, 1999, Home Oil transferred substantially all of its business assets to Home Concrete as a capital contribution. Three days later, the taxpayers (except Home Oil) transferred percentages of their respective partnership interests in Home Concrete to Home Oil as capital contributions to Home Oil. On August 31, 1999, Home Concrete sold substantially all of its assets to a third-party purchaser for $10,623,348.

In April 2000, Home Concrete and the taxpayers timely filed their tax returns for the 1999 tax year. Home Concrete elected to adjust, or "step-up," its inside basis under 26 U.S.C. ("I.R.C.") § 754 to equal the tax-

---

row to make delivery." BLACK'S LAW DICTIONARY 1456 (9th ed. 2009). To close the short sale, "'[t]he short seller is obligated . . . to buy an equivalent number of shares [or substantially identical security] in order to return the borrowed [property].'" In theory, the short seller makes this covering purchase using the funds he received from selling the borrowed [property].'" *Kornman & Assocs., Inc. v. United States*, 527 F.3d 443, 450 (5th Cir. 2008) (quoting *Zlotnick v. TIE Commc'ns*, 836 F.2d 818, 820 (3d Cir. 1988)).

[2] A partner's basis in her partnership interest is called "outside basis," and a partnership's basis in its assets is referred to as its "inside basis." *Kornman*, 527 F.3d at 456 n.12; *see also* 26 U.S.C. §§ 722-23.

payers' outside bases. *See* I.R.C. § 743(b)(1). Home Concrete then adjusted its inside basis to $10,527,350.53, including the amount of short sale proceeds earlier contributed by the taxpayers. As a result, Home Concrete reported a modest $69,125.08 gain from the sale of its assets.

Home Concrete's 1999 tax return reported the basic components of the transactions. Its § 754 election form gave, for each partnership asset, an itemized accounting of the partnership's inside basis, the amount of the basis adjustment, and the post-election basis. The sum of the post-election bases is indicated at the end of the form. On its face, Home Concrete's return also showed a "Sale of U.S. Treasury Bonds" acquired on May 18, 1999 at a cost of $7,359,043, and a sale of those Bonds on May 19, 1999 for $7,472,405. The return also reported the resulting gain of $113,362. Similarly, the taxpayers' individual returns showed that "during the year the proceeds of a short sale not closed by the taxpayer in this tax year were received."

Notwithstanding these disclosures, the Internal Revenue Service ("IRS") did not investigate the taxpayers' transactions until June 2003. The IRS issued a summons to Jenkins & Gilchrist, P.C., the law firm that assisted the taxpayers with the transactions, on June 19, 2003. The parties agree that substantial compliance with the IRS summons did not occur until at least May 17, 2004.

As a result of the investigation, on September 7, 2006 the IRS issued a Final Partnership Administrative Adjustment ("FPAA"), decreasing to zero the taxpayers' reported outside bases in Home Concrete and thereby

substantially increasing the taxpayers' taxable income. Specifically, the IRS reasoned that

> the purported partnership was formed and availed of solely for purposes of tax avoidance by artificially overstating basis in the partnership interests of its purported partners. . . . [T]he acquisition of any interest in the purported partnership by the purported partner, short sales of Treasury Notes, the transfer of proceeds from short sales of Treasury Notes or other assets to a partnership in return for a partnership interest, the purchase or disposition of assets by the partnership, and the distribution of those assets or proceeds from the disposition of those assets to the purported partners, and the subsequent sale of those assets to generate a loss, all within a period of 8 months, had no business purpose other than tax avoidance, lacked economic substance, and, in fact and substance, constitutes an economic sham for federal income tax purposes. Accordingly, the partnership and the transactions described above shall be disregarded in full and (1) any purported losses resulting from these transactions are not allowable as deductions; and (2) increases in basis of assets are not allowed to eliminate gain for federal income tax purposes.

Accordingly, Home Concrete deposited $1,392,118 with the IRS and sued in the District Court for the Eastern District of North Carolina to recover that amount, alleging that the FPAA was barred by the general three-year limitations period in I.R.C. § 6501(a).

In response, the IRS contended that the FPAA was timely under the six-year limitations period in

§ 6501(e)(1)(A). The IRS invoked the extended statute of limitations arguing that Home Concrete "omit[ted] from gross income an amount properly includable therein" and which exceeded 25% of the amount of gross income stated in Home Concrete's 1999 tax return. *Home Concrete & Supply, LLC v. United States*, 599 F. Supp. 2d 678, 683 (E.D.N.C. 2008). There was no dispute that if an amount had been omitted from Home Concrete's return, that amount exceeded the 25% threshold. Likewise, there was no dispute that the FPAA would have been timely under the six-year statute of limitations, which would have been tolled beginning six months after the date the summons issued to the date of compliance. *Id.* at 681 n.5; *see also* I.R.C. § 7609(e)(2). By the district court's calculation, "the limitations period for the 1999 tax returns was suspended from December 20, 2003, until May 17, 2004. . . . Thus, a six-year statute, tolled, would not have run even under this most restrictive interpretation of the record until" September 14, 2006. *Home Concrete & Supply*, 599 F. Supp. 2d at 681 n.5.

On the other hand, the taxpayers argued that the six-year statute of limitations was inapplicable because Home Concrete's allegedly overstated basis did not constitute an omission from gross income. And even if it had been an omission, the taxpayers argued, their tax returns collectively made adequate disclosure of the transactions such that they were entitled to the safe harbor of the three-year statute of limitations under § 6501(e)(1)(B)(ii) (hereafter "safe harbor provision"). *Id.* at 683.

Thereafter, the district court granted partial summary judgment in the IRS's favor, ruling that "where a

taxpayer overstates basis and, as a result, leaves an amount out of gross income, the taxpayer 'omits from gross income an amount properly includible therein' for purposes of § 6501(e)(1)(A)." *Id.* at 687. The court ordered further briefing on, among other issues, whether the taxpayers adequately disclosed any omitted amount such that the safe harbor provision applied. After considering the supplemental briefs,[3] the district court ruled that the taxpayers failed to make adequate disclosure and therefore could not invoke the safe harbor provision. Accordingly, the district court concluded that the FPAA was timely under the six-year statute of limitations in § 6501(e)(1)(A). Home Concrete and the taxpayers appealed.

II.

On appeal, Home Concrete and the taxpayers argue that *Colony* establishes that an overstated tax basis does not constitute an omission from gross income for purposes of extending the limitations period for assessments. We review this question of law de novo. *Blaustein & Reich, Inc. v. Buckles*, 365 F.3d 281, 286 (4th Cir. 2004)

In *Colony*, the IRS alleged that a taxpayer "understated the gross profits on the sales of certain lots of land for residential purposes as a result of having overstated the 'basis' of such lots by erroneously including in their cost certain unallowable items of development expense." 357 U.S. at 30, 78 S. Ct. 1033. The IRS fur-

[3] In their supplemental brief to the district court, the taxpayers stipulated "for purposes of resolving the [cross-motions for summary judgment] only, that 'they overstated the tax basis of the assets that [Home Concrete] sold in 1999 resulting in an omission [ ] from gross income in excess of 25 percent of the stated gross income amount.'"

ther contended that the amount left out of gross income because of the overstated basis exceeded 25% of the amount of gross income stated in the relevant tax returns. The IRS argued that its assessments were therefore timely under the extended five-year statute of limitations in former I.R.C. § 275(c). *Id.* at 30-31, 78 S. Ct. 1033. That section stated that:

> If the taxpayer omits from gross income an amount properly includable therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

26 U.S.C. § 275(c) (1939).

The Supreme Court in *Colony* acknowledged that former § 275(c) was ambiguous and did not clearly answer whether Congress intended an overstated basis to constitute an omission from gross income stated in the return. The Court found in the legislative history "persuasive evidence that Congress was addressing itself to the specific situation where a taxpayer actually omitted some income receipt or accrual in his computation of gross income, and not more generally to errors in that computation arising from other causes." *Id.* at 33, 78 S. Ct. 1033. According to the Court, "in enacting [former §] 275(c) Congress manifested no broader purpose than to give the Commissioner an additional two years to investigate tax returns in cases where, because of a taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors." *Id.* at 37, 78 S. Ct. 1033. The Court therefore

refused to construe "omits" broadly and instead restricted its applicability to situations where taxpayers actually fail to report income.

Notably, in dicta, the Supreme Court also stated that its conclusion was "in harmony with the *unambiguous* language of section 6501(e)(1)(A)"—the section at issue in this case. *Id.* (emphasis added). In 1954, Congress recodified former § 275(c) at § 6501(e)(1)(A). Congress extended the limitations period from five years to six, and added the following additional subsections:

> (i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and
>
> (ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item.

Section 6501(e)(1)(A) and former § 275(c) are otherwise essentially identical.

In this case, the district court distinguished *Colony* on the ground that its holding is limited to cases in which the taxpayer is a trade or business selling goods or services. *Home Concrete & Supply*, 599 F. Supp. 2d at 685-86; *accord, e.g., Beard v. Comm'r*, 633 F.3d 616, 620 (7th Cir. 2011) (holding that *Colony* only applies in

the trade or business context); CC & *F W. Operations Ltd. P'ship v. Comm'r*, 273 F.3d 402, 406 n.2 (1st Cir. 2001) (noting, in dicta, the "arguable implication" that the holding of *Colony* applies only to sales of goods or services by a trade or business). In doing so, the district court relied heavily upon the Court of Federal Claims' decision in *Salman Ranch, Ltd. v. United States*, 79 Fed. Cl. 189 (2007), which has since been reversed by the Federal Circuit. 573 F.3d 1362 (Fed. Cir. 2009). The Federal Circuit expressly refused to limit *Colony's* application to sales of goods or services by a trade or business because nothing in *Colony* suggests such a limitation. *Salman Ranch*, 573 F.3d at 1373; *see also Bakersfield Energy Partners, L.P. v. Comm'r*, 568 F.3d 767, 778 (9th Cir. 2009) ("There is no ground for suggesting that the [*Colony*] Court intended the same language in § 275(c) to apply differently to taxpayers in a trade or business than to other taxpayers."); *Grapevine Imports, Ltd. v. United States*, 77 Fed. Cl. 505, 511 (2007) ("[T]his court sees no basis for limiting the Supreme Court's decision [in *Colony*] to sales of goods or services by a trade or business."); *UTAM, Ltd. v. Comm'r*, 98 T.C.M. (CCH) 422, 2009 WL 3739456, at *3 (2009) (same).

Like the Ninth and Federal Circuits, we hold that the Supreme Court in *Colony* straightforwardly construed the phrase "omits from gross income," unhinged from any dependency on the taxpayer's identity as a trade or business selling goods or services. There is, therefore, no ground to conclude that the holding in *Colony* is limited to cases involving a trade or business selling goods or services. *See Salman Ranch*, 573 F.3d at 1373 ("We are not prepared to conclude—based simply upon the Court's reference to ambiguity in § 275(c)

and the lack thereof in § 6501(e)(1)(A)—that the Court's facially unqualified holding nevertheless carries with it a qualification.").

Further, the Supreme Court's discussion of the legislative history behind former § 275(c) is equally compelling with regard to current § 6501(e)(1)(A). The language the Court construed in former § 275(c)—"omits from gross income an amount properly includable therein"—is identical to the language at issue in § 6501(e)(1)(A). Because there has been no material change between former § 275(c) and current § 6501(e)(1)(A), and no change at all to the most pertinent language, we are not free to construe an omission from gross income as something other than a failure to report "some income receipt or accrual." *Colony*, 357 U.S. at 33, 78 S. Ct. 1033; *see also Bakersfield Energy Partners, L.P.*, 568 F.3d at 778 (concluding that *Colony* forecloses the argument that an overstated basis can constitute an omission from gross income for purposes of extending the statute of limitations under § 6501(e)(1)(A)); *Salman Ranch*, 573 F.3d at 1377 (same). Thus, we join the Ninth and Federal Circuits and conclude that *Colony* forecloses the argument that Home Concrete's overstated basis in its reporting of the short sale proceeds resulted in an omission from its reported gross income.

III.

The IRS presses another path around *Colony*. After concluding that the IRS's position regarding the meaning of "omits" was barred by *Colony*, the Ninth Circuit commented that the "IRS may have the authority to promulgate a reasonable reinterpretation of an ambiguous provision of the tax code, even if its interpretation runs contrary to the Supreme Court's 'opinion as to the best reading' of the provision." *Bakersfield Energy Partners*, 568 F.3d at 778 (quoting *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 982-83, 125 S. Ct. 2688, 162 L. Ed. 2d 820 (2005)).

Perhaps in response to the Ninth Circuit's cue, the IRS promulgated a temporary regulation on September 28, 2009, which became final during the pendency of this appeal. Treas. Reg. § 301.6501(e)-1. The IRS claims that this regulation is entitled to controlling deference under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 104 S. Ct. 2778, 81 L. Ed. 2d 694 (1984).

The regulation states that:

> (iii) For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to any income other than from the sale of goods or services in a trade or business, has the same meaning as provided under section 61(a), and includes the total of the amounts received or accrued, to the extent required to be shown on the return. In the case of amounts received or accrued that relate to the disposition of property, and except as provided in paragraph (a)(1)(ii) of this section, *gross income* means the excess of the amount realized from the disposi-

> tion of the property over the unrecovered cost or other basis of the property. Consequently, except as provided in paragraph (a)(1)(ii) of this section, an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A).
>
> . . .
>
> (e) *Effective/applicability date—(1) Income Taxes.* Paragraph (a) of this section applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009.

Treas. Reg. § 301.6501(e)-1(a)(1)(iii)(1)(e)(1) (2010). The IRS asks us to apply the regulation retroactively to produce the result it desires in this case. We decline to do so for several reasons.

First, the 1999 tax year at issue in this case, for which tax returns were due by April 2000, is well beyond the reach of the regulation's express period of applicability. Even assuming *arguendo* that the six-year statute of limitations applied, pursuant to the regulation, the "period for assessing tax" would have expired, according to the district court's unchallenged finding, on September 14, 2006. Thus, the period for assessing tax for the 1999 tax year expired long before September 24, 2009. By its own terms, the regulation does not apply here.[4]

---

[4] In *UTAM*, the Tax Court noted that the IRS (curiously) did not rely on the temporary regulation, even though it had been promulgated while that case was still pending. 98 T.C.M. (CCH) at * 1 n.2. We observe that the timeline in this case is virtually identical to the timeline in *UTAM*: The IRS issued an FPAA on October 13, 2006, alleging that the taxpayer had omitted gross income by overstating basis in its tax

The IRS urges a different interpretation of the regulation's applicability clause in the preamble to Treasury Decision 9511. The preamble suggests that the "six-year period for assessing tax" in § 6501(e)(1) remains open for "all taxable years . . . that are the subject of any case pending before any court of competent jurisdiction (including the United States Tax Court and Court of Federal Claims) in which a decision had not become final (within the meaning of [26 U.S.C. §] 7481)." Because this case was not finally resolved as of September 24, 2009, the IRS argues that § 6501(e)(1)'s six-year period for assessing tax remains open and Treasury Regulation § 301.6501(e)-1(e) applies. We cannot agree.

With this logic, the IRS attempts to re-draft I.R.C. § 6501. In the statute, Congress made clear that the window for tax assessments, barring special circumstances, closes after three years. I.R.C. § 6501(a). In the event of an omission, the window closes after six years. I.R.C. § 6501(e). And Congress specifically listed circumstances, such as fraud, in which the assessment window remains open without limitation. *Id.* § 6501(c). Congress unambiguously stated its intent to close the period for assessing tax within six years after a return is filed, except in cases of fraud. Accordingly, the IRS's argument that the period for assessing tax is open—or indeed may be re-opened, as would be the case here—so long as litigation is pending is contrary to the clearly and unambiguously expressed intent of Congress and must fail. *United States v. Mead*, 533 U.S. 218, 227, 121

---

return for the 1999 tax year. *Id.* at *1-2. The IRS did not ask the Tax Court to apply the temporary regulation retroactively in *UTAM* yet asks this Court to do so in this factually analogous case.

S. Ct. 2164, 150 L. Ed. 2d 292 (2001) (stating that an agency's interpretation is not binding on courts if it is "manifestly contrary to the statute"). Not surprisingly, the Tax Court rejected the same argument as to the substantially identical applicability clause in the temporary regulation. *Intermountain Ins. Servs. of Vail, LLC v. Comm'r*, 134 T.C. No. 11, 2010 WL 1838297, at *4-6 (2010) (rejecting the IRS's argument as circular and contrary to the plain language of the regulations).

Second, even putting the applicability clause aside, *Chevron* deference is warranted only when a treasury regulation interprets an ambiguous statute. *Mayo Found. for Med. Educ. & Research v. United States*, 562 U.S. —, — - —, 131 S. Ct. 704, 711, 178 L. Ed. 2d 588 (2011); *see also Brand X Internet Servs.*, 545 U.S. at 980, 125 S. Ct. 2688; *Chevron*, 467 U.S. at 842-43, 104 S. Ct. 2778. While we are aware that lower courts are divided regarding whether an overstated basis constitutes an omission from gross income, the Supreme Court's reference to "the *unambiguous* language of section 6501(e)(1)(A)" cannot be ignored. *Colony*, 357 U.S. at 37, 78 S. Ct. 1033 (emphasis added). Because the regulation here interprets "omits from gross income" under § 6501(e)(1)(A), and the Supreme Court declared that statute unambiguous, we do not believe that the regulation is entitled to controlling deference. *See Chevron*, 467 U.S. at 842-43, 104 S. Ct. 2778 ("If the intent of Congress is clear, that is the end of the matter; for the courts, as well as the agency, must give effect to the unambiguously expressed intent of Congress.").

Finally, we are not persuaded by the IRS's argument that the regulation should apply retroactively to this case as a clarification of law established in *Colony* and

other cases. The Supreme Court has acknowledged that a subsequent agency interpretation of an ambiguous statute may displace an earlier judicial construction of the same provision. *Brand X Internet Servs.*, 545 U.S. at 982-83, 125 S. Ct. 2688. But again, the Supreme Court stated in *Colony* that § 6501(e)(1)(A) is unambiguous as to the very issue to which the regulation purports to speak. The regulation is not, therefore, a mere clarification. Rather, if applied, the regulation would change the law governing the taxpayers' 1999 tax returns and thereby subject the taxpayers to liability to which they would not have been subject under pre-regulation law. *See United States v. Capers*, 61 F.3d 1100, 1110 (4th Cir. 1995) (declining to apply an amendment to the United States Sentencing Guidelines retroactively because the amendment changed Fourth Circuit law so as to deprive the defendant of a benefit to which he would have been entitled under pre-amendment law).

Because *Colony* was established law when the taxpayers filed their returns in April 2000, we refuse to apply Treasury Regulation § 301.6501(e)-1(e), which purports to establish a rule contrary to *Colony* to subject the taxpayers to the extended limitations period ten years later. *See Levy v. Sterling Holding Co.*, 544 F.3d 493, 506 (3d Cir. 2008) ("[W]here a new rule constitutes a clarification—rather than a substantive change—of the law as it existed beforehand, the application of that new rule to pre-promulgation conduct necessarily does *not* have an impermissible retroactive effect"); *cf. Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 744 n.3, 116 S. Ct. 1730, 135 L. Ed. 2d 25 (1996) (stating that an agency interpretation does not have an impermissible retroactive effect where there was previously no clear agency guidance).

IV.

In sum, we conclude that the Supreme Court's holding in *Colony* applies to § 6501(e)(1)(A). An overstated basis in property is not an omission from gross income that extends the limitations period in § 6501(e)(1)(A). Accordingly, Home Concrete's overstated basis in the short sale proceeds did not trigger the six-year statute of limitations. Moreover, Treasury Regulation § 301.6501(e)-1(e), by the plain terms of its applicability clause, does not apply to the tax year at issue in this case and is furthermore not entitled to deference. The general three-year statute of limitations in § 6501(a) applies, making the FPAA here untimely. We reverse the district court's judgment to the contrary.[5]

REVERSED.

WILKINSON, Circuit Judge, concurring:

I am happy to concur in Judge Wynn's fine opinion in this case. The *Chevron* test is straightforward enough when it comes to post-*Chevron* cases. But it is sometimes difficult to determine whether pre-*Chevron* decisions are based upon "*Chevron* step one" (the plain command of the statute) or upon "*Chevron* step two" (a permissible construction of the statute). *Mayo Found. for Med. Educ. & Research v. United States*, 562 U.S. —, — - —, 131 S. Ct. 704, 711, 178 L. Ed. 2d 588 (2011). Certainly Justice Harlan in *Colony, Inc. v. Commissioner*, 357 U.S. 28, 78 S. Ct. 1033, 2 L. Ed. 2d 1119 (1958), had no occasion to ponder the permutations of the *Chevron* test, which came down in 1984.

---

[5] In light of this holding, we need not reach the parties' arguments regarding the safe harbor provision.

Here, however, I am persuaded that the Supreme Court rested its judgment in *Colony* on the plain language of the statute, which then, as now, stated that the extended statute of limitations for assessing tax liability applies "[i]f the taxpayer *omits* from gross income an amount properly includible therein." 26 U.S.C. § 275(c) (1939) (emphasis added); *see* 26 U.S.C. § 6501(e)(1)(A) (current version). In other words, I believe that *Colony* was decided under *Chevron* step one.

Lawyers of course are adept at finding ambiguity, and language of course is by its nature imprecise. One need not consult a dictionary, however, to understand that the plain meaning of "omit" is "to leave out" or "to fail to mention." The taxpayers here did not omit, leave out, or fail to mention their transaction. Instead, they provided the details on their returns. *See* Majority Op. at 252. To be sure, the IRS asserts that the returns overstated Home Concrete's basis and thus understated the overall tax liability resulting from the sale of its assets. But as the Court noted in *Colony*, if Congress had been concerned with that problem, "it could have chosen another verb such as 'reduces' or 'understates,' either of which would have pointed significantly in the Commissioner's direction." *Colony*, 357 U.S. at 32, 78 S. Ct. 1033.

I recognize there is some language in *Colony* suggesting that the Court looked at legislative history or thought that § 275(c) was ambiguous. *See Colony*, 357 U.S. at 33, 78 S. Ct. 1033 ("Although we are inclined to think that the statute on its face lends itself more plausibly to the taxpayer's interpretation, it cannot be said that the language is unambiguous. In these circumstances we turn to the legislative history of § 275(c).").

But that language seems to me secondary in importance to the thrust of the opinion and to the Court's argument that "in enacting § 275(c) Congress manifested no broader purpose than to give the Commissioner [additional time] to investigate tax returns in cases where, because of a taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors." *Id.* at 36, 78 S. Ct. 1033. More importantly, as Judge Wynn notes, the Court observed that its decision was "in harmony with the *unambiguous* language of" 26 U.S.C. § 6501(e)(1)(A), the successor provision to § 275(c) and the provision at issue here. *See id.* at 37, 78 S. Ct. 1033 (emphasis added).

I appreciate that *Chevron* and *National Cable & Telecommunications Ass'n v. Brand X Internet Services*, 545 U.S. 967, 125 S. Ct. 2688, 162 L. Ed. 2d 820 (2005), afford agencies considerable discretion in their areas of expertise. As *Brand X* put it, "*Chevron* established a presumption that Congress, when it left ambiguity in a statute meant for implementation by an agency, . . . desired the agency (rather than the courts) to possess whatever degree of discretion the ambiguity allows." *Brand X*, 545 U.S. at 982, 125 S. Ct. 2688 (internal quotations and citation omitted). The Supreme Court's recent decision in *Mayo Foundation* likewise affords full *Chevron* deference to Treasury Regulations, concluding that the Treasury Department's interpretations of ambiguous statutes will stand if they are "a 'reasonable interpretation' of the enacted text." *Mayo Found.*, 562 U.S. at —, 131 S. Ct. at 714 (quoting *Chevron*, 467 U.S. at 844, 104 S. Ct. 2778). Given the fact that government today is an enterprise of unprecedented complexity, this makes perfect sense. Nor do judges

harbor any desire to impair the mission of the IRS in a day of staggering budget deficits.

Yet it remains the case that agencies are not a law unto themselves. No less than any other organ of government, they operate in a system in which the last words in law belong to Congress and the Supreme Court. What the IRS seeks to do in extending the statutory limitations period goes against what I believe are the plain instructions of Congress, which have not been changed, and the plain words of the Court, which have not been retracted. *See Colony*, 357 U.S. at 37, 78 S. Ct. 1033.

This seems to me something of an inversion of the universe and to pass the point where the beneficial application of agency expertise gives way to a lack of accountability and a risk of arbitrariness. We do not stand alone in reaching this determination; other courts have similarly rebuffed the IRS's repeated attempts to adopt the six-year statute of limitations for omissions of gross income so as to cover misleading statements in tax returns that would result in tax deficiencies. *See Salman Ranch Ltd. v. United States*, 573 F.3d 1362, 1372-74 (Fed. Cir. 2009); *Bakersfield Energy Partners, L.P. v. Comm'r*, 568 F.3d 767, 778 (9th Cir. 2009); *Grapevine Imports, Ltd. v. United States*, 77 Fed. Cl. 505, 511-12 (2007); *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 134 T.C. No. 11, 2010 WL 1838297, at *6-8 (2010). These courts have recognized that regardless of whether the IRS's position is sound as a matter of policy, it is simply not the law.

We have been told many times to leave to the Court "the prerogative of overruling its own decisions." *See Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490

U.S. 477, 484, 109 S. Ct. 1917, 104 L. Ed. 2d 526 (1989). If that injunction has been issued to the circuit courts, it assuredly applies to agencies in situations where the Court has interpreted the plain language of a statutory command. Maybe Congress will conclude at some point that the six-year period should apply to declarations that fall short of omissions or the Court may decide that *Colony* was somehow, after all, a *Chevron* step two case. But those decisions are neither ours nor the agency's to make. *Chevron*, *Brand X*, and more recently, *Mayo Foundation* rightly leave agencies with a large and beneficial role, but they do not leave courts with no role where the very language of the law is palpably at stake. There is a balance to be struck here, and courts still must play a part in determining where "here" is. The disruption of that balance in this case seems clear and evident.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 09-2353
(7:06-cv-00181-FL)

HOME CONCRETE & SUPPLY, LLC; ROBERT L. PIERCE; STEPHEN R. CHANDLER; REBECCA R. CHANDLER; HOME OIL AND COAL COMPANY, INCORPORATED; SUSANNE D. PIERCE,
PLAINTIFFS-APPELLANTS

v.

UNITED STATES OF AMERICA, DEFENDANT-APPELLEE

BAUSCH & LOMB, INC., AMICUS SUPPORTING APPELLANT

Filed: Apr. 5, 2011

ORDER

The petition for rehearing en banc was circulated to the full court. No judge requested a poll under Fed. R. App. P. 35. The court denies the petition for rehearing en banc.

For the Court

/s/ PATRICIA S. CONNOR, CLERK
PATRICIA S. CONNOR

APPENDIX C

UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF NORTH CAROLINA, SOUTHERN DIVISION

No. 7:06-CV-181-FL

HOME CONCRETE & SUPPLY, LLC, A DELAWARE LIMITED LIABILITY COMPANY; ROBERT L. PIERCE, AS TAX MATTERS PARTNER; SUSANNE D. PIERCE; STEPHEN R. CHANDLER; REBECCA R. CHANDLER; AND HOME OIL AND COAL COMPANY, INC., A NORTH CAROLINA CORPORATION, PLAINTIFFS/PETITIONERS

v.

UNITED STATES OF AMERICA, DEFENDANT/RESPONDENT

Filed: Nov. 21, 2008

ORDER

LOUISE W. FLANAGAN, Chief Judge.

Plaintiffs/petitioners ("plaintiffs") initiated this action by filing "Complaint and Petition for Readjustment of Partnerships Items Under 26 U.S.C. § 6226," wherein they seek a determination that any tax assessment for the 1999 tax year is time barred and that no adjustment of their taxes is warranted for the 1999 tax year. Plaintiffs include Home Concrete & Supply, LLC, ("Home

Concrete"), a Delaware limited liability company which is deemed a partnership, and its owners who are deemed partners, for federal income tax purposes.[1] Plaintiffs also include Robert L. Pierce ("Pierce"), the tax matters partner for Home Concrete, who seeks reimbursement of the sum of $1,392,118.00[2] he deposited with the IRS, together with his wife, plaintiff Susanne D. Pierce, with whom he filed jointly for the 1999 tax year. Pierce owned Home Oil & Coal Company, Inc. ("Home Oil") at the time of its 1999 sale together with plaintiff Stephen R. Chandler ("Chandler"), who proceeds here also with his wife, Rebecca R. Chandler, with whom he filed jointly for that tax year. Home Oil also is a plaintiff in this action.

---

[1] While the government denied in its first amended answer treatment as a partnership to Home Concrete for tax purposes, (Def.'s First Am. Answer, ¶ 2), this denial appears to have no basis in fact or law, and, moreover, to have been discounted by defendant in subsequent filings. Pursuant to 26 C.F.R. §§ 301.7701-2 and 301.7701-3, a limited liability company such as Home Concrete by default receives pass-through partnership tax treatment unless it elects to change its tax status by filing a Form 8832 "Entity Classification Election" with the Internal Revenue Service ("IRS"). *See* 26 C.F.R. §§ 301.7701-2 and 301.7701-3. None of the numerous exhibits proffered by the government includes a Form 8832 for Home Concrete electing to receive federal corporate tax treatment. Indeed, all of the documents offered by both parties indicate that plaintiff Home Concrete did, in fact, receive pass-through partnership tax treatment from the IRS. This, of course, would include the Notice of Final Partnership Administrative Adjustment ("FPAA"), underlying the instant action.

[2] This amount represents the amount by which the partnership's tax liability would be increased if the treatment of partnership items on Home Concrete's return were made consistent with the treatment of partnership items on the partnership return as defined by the FPAA issued by the Internal Revenue Service ("IRS") September 7, 2006.

The case comes now before the court on plaintiffs' motion for summary judgment and defendant's motion for partial summary judgment, presenting for decision the question of whether a three year or a six year limitations period applies for any IRS assessments relating to the transactions at issue.

STATEMENT OF THE CASE

Plaintiffs filed the instant action pursuant to 26 U.S.C. § 6226(e)(1), seeking refund of deposit made for the 1999 tax year in response to the 2006 FPAA. Plaintiffs allege that the 2006 FPAA was time barred by the three year statute of limitations in §§ 6229[3] and 6501. Plaintiffs allege further that the IRS assessments are erroneous and disclaim any liability. Defendant asserts in response that the six year limitations period prescribed in § 6501(e)(1)(A) applies and plaintiffs are not entitled to refund of the deposit. It is the government's position that the assessments are proper.

On February 23, 2007, plaintiffs moved for judgment on the pleadings, asserting, as they do now, that defendant's assessment of taxes for the 1999 tax year was time barred because the three year limitations period set forth in § 6501(a) applies to any action to recover taxes related to their 1999 tax returns. The six year statute of limitations provided by § 6501(e)(1)(A) in this case applies, the government argued then and argues now, because plaintiffs omitted a substantial amount of gross income from their returns. As set forth in prior order, after protracted briefing, the court denied, with-

---

[3] Plaintiffs seemingly discount applicability now of § 6229 as no mention is made in their briefing on the instant motions. The three year statute of limitations at issue is the one set forth in § 6501.

out prejudice, plaintiffs' motion for judgment on the pleadings and defendant's motion for partial summary judgment. An agreed to case schedule was implemented, including limited discovery, and on this basis the parties' cross-motions come now before the court.

In their motion for summary judgment, plaintiffs argue that the FPAA is time barred by 26 U.S.C. § 6501(a), which sets out a general three year statute of limitations for actions to assess taxes on partnerships and individuals. Defendant moves for partial summary judgment, on grounds that the six year statute of limitations provided by § 6501(e)(1)(A) applies to tax assessments based on the plaintiffs' 1999 tax returns under the circumstances presented, and the assessment therefore was timely.

STATEMENT OF UNDISPUTED FACTS

On the record presented, the specific date of filing of the partners' individual returns, which the parties agree, for purposes of beginning the §§ 6501(a) and (e) limitations periods, are the relevant ones, *see Bufferd v. C.I.R.*, 506 U.S. 523, 526, 113 S. Ct. 927, 122 L. Ed. 2d 306 (1993), is unclear. However, for purposes of calculating the § 6501 limitations periods, the actual date of filing of a return does not matter, as long as the return is filed before the deadline. *See* 26 U.S.C. § 6501(b)(1). The date used as the date of "filing" for returns filed before the deadline is the deadline date. There is no dispute that the returns at issue were filed before the April 17, 2000, deadline.

On the record before the court, there also is no issue that June 19, 2003, the IRS served summons pursuant to court order on Jenkens & Gilchrist, P.C. ("Jenkens"),

plaintiffs' attorneys, well within the six year statute of limitations asserted by the government.[4] Though the record is unclear as to the precise date that Jenkens responded to the summons related to Home Concrete, the parties agree that the earliest possible date of compliance was May 17, 2004. It is undisputed that the IRS issued the FPAA assessing the contested taxes on September 7, 2006, more than six years after the April 17, 2000 filing date.[5]

The FPAA assessing the taxes contested by plaintiffs was issued in response to a series of transactions undertaken by plaintiffs Pierce and Chandler in anticipation of the sale of the business, Home Oil. Following the advice of their accountants, Arthur Andersen LLP, and Jenkens, plaintiffs embarked on a series of transactions

---

[4] There is reference in defendant's first amended answer to issuance of a summons on May 21, 2002; however, there is nothing in the record showing service of a summons issued on this date nor does any summons with this date play a part on the parties' arguments to the court.

[5] There appears no dispute, however, that the FPAA issued within a six year statute of limitations period running from April 17, 2000 to September 14, 2006 which accounts for tolling of the limitations period provided by 26 U.S.C. § 7609(e). Plaintiffs do not dispute that § 7609(e) provides a mechanism by which the applicable time limit is tolled where a party having "possession, custody, or care of books of account containing entries relating to the business of the person liable" for a given tax, 26 U.S.C. § 7602(a)(2), receives a summons from the IRS but fails to respond within six months of the summons. 26 U.S.C. § 7609(e)(2). As noted above, plaintiffs' attorneys received such a summons and failed to respond within six months. As a result it appears the limitations period for the 1999 tax returns was suspended from December 20, 2003, until May 17, 2004. Thus, a six year statute, tolled, would not have run even under this most restrictive interpretation of the record until a few days after the FPAA was issued.

including short sales[6] designed to increase basis in certain assets, thus decreasing income tax liability from the sale of the business.[7] Plaintiffs contend an increased basis for Pierce and Chandler in Home Concrete resulted equal to the amount of the proceeds from the short sales with no offset for the obligations to close the short sales. The IRS contends that the proper treatment of the capital contributions at issue would include

---

[6] Short sales are transactions that provide a twist on "buy low, sell high" where the first step is to "sell high" and the last step is to "buy low." In a short sale transaction, an investor borrows shares, or in this case U.S. Treasury Notes from a brokerage house and sells them in the open market. The proceeds from this sale go into the investor's account with the brokerage house. At some point later, the investor must replace the borrowed shares or notes by purchasing new ones. If the short seller is successful, he will be able to purchase the shares at a lower price than those he sold, allowing him to take a profit on the transaction.

[7] It appears that on April 15, 1999, plaintiffs created three entities for purposes of carrying out their transactions: Home Concrete; Salisbury Investments LLC, ("Salisbury"), a single member Delaware limited liability company owned by Pierce; and Goodnight Investments LLC, ("Goodnight"), a single member Delaware limited liability company owned by Chandler. On May 13, 1999, using Salisbury, Goodnight and two trusts owned and controlled by Pierce, Pierce and Chandler initiated several short sales of U.S. Treasury Notes. Four days later, on May 17, 1999, Pierce and Chandler contributed the proceeds from all of the short sales, along with margin cash, to Home Concrete as a capital contribution. Critically, also on May 17, 1999, Pierce and Chandler contributed the obligations to close the short sales to Home Concrete. The next day, on May 18, 1999, Home Concrete covered the short sale positions. It appears that on June 11, 1999, Home Oil transferred all of its business assets to Home Concrete as a capital contribution. Then, on June 14, 1999, Pierce and Chandler each transferred substantially all of their respective ownership interests in Home Concrete to Home Oil as capital contributions. These transfers included the basis plaintiffs claim the May 17, 1999, transfers created in Home Concrete.

the obligations to close the short sales as a liability offsetting the contributions and, therefore, the contributions produced no increase in basis.

According to plaintiffs' calculation, because of the basis claimed by the plaintiffs from the short sales, Home Oil's basis in its partnership interest in Home Concrete exceeded the amount of its share of Home Concrete's basis in its assets by the amount of basis claimed from those transactions. Plaintiffs elected to take advantage of 26 U.S.C. § 754, which allows partnerships to increase the partnership's basis in its assets to equal the partners' basis in the partnership. The parties agree that, using this election, Home Oil claimed an increased basis in Home Concrete of $5,984,526.17. This apparently produced a total basis in Home Concrete's assets of approximately $10,527,350.00, though, again, the record does not appear particularly precise on this point.

On August 31, 1999, Home Concrete sold substantially all of its assets to a third party for $10,623,348.00. Plaintiffs claim this resulted in only a modest gain for Home Concrete. Defendant claims that, because the stepped up basis claimed by plaintiffs was impermissible, Home Concrete realized a substantially greater amount of taxable gain. Ultimately, defendant issued the September 7, 2006, FPAA assessing taxes on the amount plaintiffs allegedly omitted from gross income, and thereafter the instant dispute was presented to the court.

DISCUSSION

Summary judgment is appropriate, under Rule 56(c), "if the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the movant is entitled to a judgment as a matter of law." FED. R. CIV. P. 56(c). A fact is material if it might affect the outcome of the case. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986). In deciding a motion for summary judgment, the court construes evidence in the light most favorable to the nonmoving party and draws all reasonable inferences in the nonmovant's favor. *Anderson*, 477 U.S. at 255, 106 S. Ct. 2505.

A party seeking summary judgment "bears the initial responsibility of informing the district court of the basis for its motion, and identifying those portions of the [record] which it believes demonstrate the absence of a genuine issue of material fact." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986). Once the moving party has met its burden, the non-moving party must then "set forth specific facts showing that there is a genuine issue for trial." *Matsushita Elec. Indus. Co. Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 586-87, 106 S. Ct. 1348, 89 L. Ed. 2d 538 (1986) (quoting FED. R. CIV. P. 56(e)).

While both sides frame the question presented as whether the three year statute of limitations in § 6501(a) or the six year statute of limitations in § 6501(e)(1)(A) applies to plaintiffs' situation, because plaintiffs contend that none of the assessments on their face are proper, consideration now of whether § 6501(e)(1)(A) applies is more complicated. Section 6501(e)(1)(A) provides that

if a taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return," the extended statute of limitations for assessments of tax by the IRS is triggered. 26 U.S.C. § 6501(e)(1)(A). So determining whether an item has been omitted in this case, where the alleged omission is an overstatement of basis, requires this court first to decide whether such an overstatement can constitute an omission under § 6501(e)(1)(A). Assuming that it does, the court then must determine whether the basis in question actually was overstated. *Id.* And if it was, before the court can decide finally whether the six year limitations period applies, it must decide whether plaintiffs adequately disclosed the omitted amount on the relevant tax returns where "[i]n determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item." 26 U.S.C. § 6501(e)(1)(A)(ii).

Plaintiffs bear the burden of initially showing that the IRS failed to assess the 1999 taxes within the three year statute of limitations asserted. *See Hoffman v. C.I.R.*, 119 T.C. 140, 146, 2002 WL 31113898 (T.C. 2002). Because it is undisputed in this case that the IRS did not assess the 1999 taxes within a three year limitations period, plaintiffs have established their prima facie case. The court's focus turns very quickly now to whether defendant can go forward under the six year limitations period, where the burden shifts to defendant to establish that § 6501(e)(1)(A)'s extended limitations period applies. *Id.*

Plaintiffs urge that *The Colony, Inc. v. Commissioner of Internal Revenue*, 357 U.S. 28, 78 S. Ct. 1033, 2 L. Ed. 2d 1119 (1958), controls this court's decision, and precludes application of the six year limitations period. Defendant contends with equal vigor that it does not. *Colony* applied an earlier version of the Internal Revenue Code (IRC), where the Court was interpreting 26 U.S.C. § 275(c), appearing in the 1939 IRC, to the case of a taxpayer who erroneously understated the gross profits from the sale of trade goods (undeveloped lots of land) by improperly increasing the basis it held in those goods. *Colony*, 357 U.S. at 31-32, 78 S. Ct. 1033. The Court began by noting that the question before it had been "resolved for future cases by Congress's adoption of § 6501(e)(1)(A)" in the 1954 IRC. *Id.* at 32, 78 S. Ct. 1033.

The Court looked at the language of § 275(c), noting the dictionary definition of "omit" as "'to leave out or unmentioned; not to insert, include, or name.'" *Id.* at 32-33, 78 S. Ct. 1033 (quoting Webster's New International Dictionary (2d ed. 1939)). However, after reviewing the text of the statute, the Court determined that "it cannot be said that the [subsection's] language is unambiguous." *Id.* at 33, 78 S. Ct. 1033. The Court reviewed the legislative history of 26 U.S.C. § 275 and found that "Congress manifested no broader purpose than to give the Commissioner an additional two years to investigate tax returns in cases where, because of a taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors." *Id.* at 36, 78 S. Ct. 1033. Thus, the Court held that the taxpayer's overstatement of basis did not trigger the extended statute of limitations provided by § 275(c), a result the Court

deemed "in harmony with the unambiguous language of § 6501(e)(A)(1)." *Id.* at 37, 78 S. Ct. 1033.

In the years since *Colony* was decided, a handful of courts have applied its holding regarding overstatements of basis to § 6501(e)(1)(A), with unharmonious results. At least four courts have found the holding of *Colony* limited to situations in which the taxpayer is a trade or business engaged in the sale of goods or services and has overstated basis in those goods or services on its return, thereby under-reporting gross income. *See Burks v. United States*, No. 3:06-CV-1747 (N.D. TX. June 13, 2008); *Brandon Ridge Partners v. United States*, 2007 WL 2209129 (M.D. Fla. 2007); *Salman Ranch, Ltd. v. United States*, 79 Fed. Cl. 189 (2007); *Phinney v. Chambers*, 392 F.2d 680 (5th Cir. 1968); *see also CC & F Western Operations Limited Partnership v. Comm'r*, 273 F.3d 402, 406 n.2 (1st Cir. 2001) (addressing a different situation but noting that § 6501(e)(1)(A)(i)'s definition of gross income for § 6501 arguably implies "that it does not apply under section 6501 to other types of income"). These courts have also held that, in non-trade and business sale of goods and services settings, a taxpayer can "omit" gross income by overstating basis.

At least three other courts have taken a more expansive view of the holding of Colony and found that the Court's interpretation of the predecessor to § 6501(e)(1)(A) applies equally to all taxpayers, regardless of whether they are a trade or business selling goods and services. *See Wilmington Partners L.P. et al. v. Comm'r*, No. 15098-06 (T.C. Apr. 30, 2008) (following *Bakersfield*); *Bakersfield Energy Partners, LP v. Comm'r*, 128 T.C. 207, 2007 WL 1712543 (2007); *Grape-*

vine Imports, Ltd. v. United States, 77 Fed. Cl. 505 (2007). Plaintiffs ask for this court to follow this line of reasoning and hold that *Colony*'s reach extends to all situations involving § 6501(e)(1)(A) so that if a taxpayer overstates basis and therefore under reports gross income, the three year statute of limitations for assessing deficiencies in tax payments still applies, regardless of whether the overstatement and omitted gross income are readily apparent on the face of the return. *See Bakersfield*, 128 T.C. at 214; *Grapevine*, 77 Fed. Cl. at 510-11. "Omit" means that § 6501(e)(1)(A) only applies when an item is completely left off of the face of a tax return, it is urged here. *See Bakersfield*, 128 T.C. at 215; *Grapevine*, 77 Fed. Cl. at 511-12. While these decisions are supportive of plaintiffs' position, the undersigned is compelled to conclude they are, in this regard, erroneous.

It is correct to say that the language of § 275(c) is virtually identical to a portion of § 6501(e)(1)(A). However, that language was found in *Colony* to be sufficiently ambiguous that the Court had to review legislative history to decide the meaning of the statute. *Colony*, 357 U.S. at 33-35, 78 S. Ct. 1033. A careful reading of the 1958 decision discloses that the word "omit" was discerned as part of the phrase "omits from gross income an amount properly includible therein" and in light of the legislative history of § 275(c). In *Colony*, the Court was applying the 1939 IRC then in effect to income tax returns for the years 1946 and 1947. The 1954 IRC effective at the time the opinion was rendered included the language of § 6501(e) as it appears today. For the Court's decision to be "in harmony" with § 6501(e)(1)(A), the transformation of the language of § 275(c)—the language that is repeated in

§ 6501(e)(1)(A)—from ambiguous to unambiguous must be tied to the two new subsections Congress added in § 6501(e)(1)(A). *See Salman Ranch*, 79 Fed. Cl. at 199 (finding that the "in harmony" language of *Colony* must be related to the two new subsections of § 6501(e)(1)(A)).

The two subsections Congress added to § 275(c) in drafting § 6501(e)(1)(A), acknowledged by the Court in *Colony*, make clear the limit of its holding. Subsection (i) redefines gross income for purposes of § 6501(e)(1)(A) in cases involving a trade or business. That subsection provides:

> (i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services.

26 U.S.C. § 6501(e)(1)(A)(i). The normal calculation for gross income for trade or business taxpayers involved in the sale of goods or services involves subtracting the cost of goods sold ("COGS") from the gross receipts of the sales. *See Salman Ranch*, 79 Fed. Cl. at 199 (quoting *In re Lilly*, 76 F.3d 568, 572 (4th Cir. 1996) (holding, in a different context, that overstatement of COGS was an "item omitted from gross income under I.R.C. § 6013(e)(1)(A)")). As the court in *Salman Ranch* cogently explained:

> [S]ection 6501(e)(1)(A)(i) provides an exception to the customary definition of gross income in the event of sales of goods or services by a trade or business, allowing that "gross income," as used in section 6501(e)(1)(A), will be defined as the "gross receipts"

> alone of those sales. Under I.R.C. § 6501(e)(1)(A), in order for an omission from gross income to arise in the context of sales of goods or services by a trade or business (which under the I.R.C. § 6501(e)(1)(A)(i) gross receipts provision actually should read "omits from gross 'receipts'"), an omission of a receipt must occur. The *Colony* Court's declaration that section 275(c) is "limited to situations in which specific receipts or accruals of income items are left out of the computation of gross income" makes eminent sense because The Colony, Inc. was a trade or business selling goods or services. *Colony*, 357 U.S. at 33, 78 S. Ct. 1033. The Court's conclusion that The Colony, Inc. had not omitted any gross income and thus was not liable under section 275(c) is "in harmony with the unambiguous language of § 6501(e)(1)(A)," in that the resolution would be the same under either provision. *Id.* at 37, 78 S. Ct. 1033.

Salman Ranch, 79 Fed. Cl. at 199.

Plaintiffs seemingly accept that for the Court's "in harmony" statement in *Colony* to make sense the "harmony" must come from somewhere in the new subsections of § 6501(e)(1)(A). However, plaintiffs urge that subsection (i) is not what creates "harmony" between the Court's holding and § 6501(e)(1)(A). Instead, plaintiffs urge this court to focus on subsection (ii) as "the obvious source of unambiguous language alluded to by the Supreme Court in *Colony*." (Mem. in Supp. of Pls.' Mot. for Summ. J. (DE # 53) at 14.) That subsection provides:

> (ii) In determining the amount omitted from gross income, there shall not be taken into account any

> amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item.

26 U.S.C. § 6501(e)(1)(A)(ii). From this language, plaintiffs draw the conclusion that the Court was referencing subsection (ii) because it deals with what it means to "omit" something from a return. Therefore, *Colony* must stand for the proposition that "omit" only means to leave an item or amount off the face of a return.[8]

Plaintiffs misapprehend the import of subsection (ii). That subsection does speak to what it means to "omit" an amount from gross income on a return. However, nothing in the language of § 6501(e)(1)(A)(ii) supports the conclusion that the only way to "omit" an item is to leave it completely off of the face of a return. Quite to the contrary, the language of subsection (ii) indicates that Congress intended for it to be possible to "omit" an item from gross income under § 6501(e)(1)(A) without leaving it completely off the face of a return. *See Phinney*, 392 F.2d at 685 (holding that subsection (ii) "makes it apparent that the six year statute is intended to apply

---

[8] Plaintiffs' focus on subsection (ii) and their reading of *Colony* would render subsection (i) superfluous. *See Salman Ranch*, 79 Fed. Cl. at 200 ("Plaintiffs' construction of this critical term 'omits' without reference to the term 'gross income' focuses only on one component of the calculation, thereby excluding consideration of one of the two figures that generates the gain—the calculation of basis—and in tandem rendering the gross receipts provision of I.R.C. § 6501(e)(1)(A)(i) superfluous."). Such a result violates a fundamental canon of statutory construction and should be avoided wherever possible. *Alaska Dept. of Envtl. Conservation v. E.P.A.*, 540 U.S. 461, 489 n.13, 124 S. Ct. 983, 157 L. Ed. 2d 967 (2004).

where there is either a complete omission of an item of income of the requisite amount or misstating the nature of an item of income which places the 'commissioner . . . at a special disadvantage in detecting errors'" (emphasis omitted)).

Subsection (ii) clearly directs that, when determining what has been omitted from gross income, no "amount which is omitted from gross income stated in the return" may be considered "if such amount is disclosed in the return . . . in a manner adequate to apprise the Secretary of the nature and amount of such item." 26 U.S.C. § 6501(e)(1)(A)(ii). Thus, from the plain language of (ii), it is possible for an amount to be "omitted from gross income" and disclosed on the face of the return. Subsection (ii) simply makes it possible for a taxpayer to be protected if the taxpayer discloses the amount in a way sufficient to alert the IRS to the substance and size of the item omitted. If a taxpayer omits an amount from gross income yet includes the item which causes the amount to be omitted on the taxpayer's return in such a way that the IRS is apprised of the "nature and amount" of the item, then that item is not considered "omitted" for purposes of § 6501(e)(1)(A). However, where a taxpayer includes an item on a return in such a way that the IRS is not apprised of the "nature and amount" of the item, then that item has been "omitted" from gross income for purposes of § 6501(e)(1)(A), even though it is included on the face of the return.

It is also instructive to consider § 6501(e)(1)(A)'s language and terms in light of the relevant statutory definitions provided by the IRC. These statutory definitions further undermine the overly broad reading of *Colony* urged by plaintiffs. "Gross income" is, broadly con-

strued,[9] "all income from whatever source derived, including . . . (3) gains derived from dealings in property." 26 U.S.C. § 61(a). Section 1001(a) fleshes out the meaning of "gains derived from dealings in property," defining gains from dealings in property as "the excess of the amount realized therefrom over the adjusted basis." 26 U.S.C. § 1001(a). Thus, "gross income" as related to dealings in property is defined with reference to the property's adjusted basis. Any overstatement in basis will necessarily decrease the amount of gross income that a taxpayer states on his return. In other words, by overstating basis in the gross income calculation, the taxpayer "leave[s] out" or fails to "include" "an amount properly includible therein." Therefore, where a taxpayer incorrectly states an overestimated basis in property, the taxpayer "omits" gross income by leaving the amount out of gross income stated on the taxpayer's return.

For all of these reasons, this court finds that where a taxpayer overstates basis and, as a result, leaves an amount out of gross income, the taxpayer "omits from gross income an amount properly includible therein" for purposes of § 6501(e)(1)(A). Therefore, the extended six year statute of limitations may apply to such a taxpayer if the taxpayer overstated basis on an item resulting in an omission from gross income of an amount properly includible therein which is in excess of the 25 percent threshold and the taxpayer does not qualify for the safe harbor provisions provided by § 6501(e)(1)(A)(ii). In this part, plaintiff's motion for summary judgment is denied,

---

[9] Gross income as defined in 26 U.S.C. § 61(a) is always to be broadly construed. *See Comm'r v. Glenshaw Glass Co.*, 348 U.S. 426, 429-30, 75 S. Ct. 473, 99 L. Ed. 483 (1955).

and in corresponding part, defendant's motion is allowed.

The court next must determine whether the basis in question actually was overstated in order to decide whether the extended limitations period applies here. Section 6501(e)(1)(A), as set forth earlier, provides that if a taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return," the extended statute of limitations for assessments of tax by the IRS is triggered. 26 U.S.C. § 6501(e)(1)(A). So determining whether an item has been omitted in this case, where the alleged omission is an overstatement of basis, requires this court first to decide whether such an overstatement can constitute an omission under § 6501(e)(1)(A), which question the court has answered in the affirmative. Before the court can decide finally whether the six year limitations period applies, it must decide whether plaintiffs adequately disclosed the omitted amount on the relevant tax returns, where "[i]n determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item." 26 U.S.C. § 6501(e)(1)(A)(ii).

The parties have presented some arguments regarding plaintiffs' disclosures for purposes of § 6501(e)(1)(A)(ii)'s safe harbor provision. Plaintiffs would say they come within its protection, and also for this reason defendant's assessment action was untimely. Defendant would have the court find they do not and, for

this reason, the six year limitations period must be applied.

To get to this part of the analysis it must be found that an omission of gross income has actually occurred in this case. And this goes to the heart of this case, making, as alluded to earlier, consideration, as a preliminary matter, whether § 6501(e)(1)(A) applies a more complicated determination than how each side now explains it. In order for the safe harbor of § 6501(e)(1)(A)(ii) to apply, plaintiffs must have disclosed the amount omitted from gross income "in a manner adequate to apprise the Secretary of the nature and amount" of the omission. 26 U.S.C. § 6501(e)(1)(A)(ii).

The court has, for the reasons given, decided as a matter of law that the six year limitations period may apply; however, the court leaves open the remaining issues presented for decision bearing on applicability of the extended limitations period pending supplemental briefing expressly on: 1) whether plaintiffs overstated basis; and, if so, 2) can the court, on the record before it, now determine whether the resulting omission from gross income was or was not in excess of 25 percent of the stated gross income amount; and, if it was 3) whether the safe harbor of § 6501(e)(1)(A)(ii) applies here. The court specifies below parameters of the briefing requested to be provided, on the facts now a part of the record.

The issue of what tax returns may be considered by the court in determining what plaintiffs did or did not disclose need not wait to be decided, however. Another legal issue susceptible now to being decided at this juncture is what standard should be used in determining whether a disclosure is adequate for purposes of

§ 6501(e)(1)(A)(ii). Resolution of these issues now will result in more focused supplemental briefing. The court sets out below the answers to these question of law bearing on whether, in this instance, if the taxpayer omitted from gross income an amount properly includible therein which is in excess of the 25 percent threshold, there was adequate disclosure.

First, as to the issue of what tax returns may be considered, section 6501(a) defines what a "return" is for purposes of that section. The case law, before the 1997 amendment to this section, interpreting what tax returns could be considered in determining adequate disclosure under § 6501(e)(1)(A)(ii), allowed courts to consider the returns of pass-through entities such as a partnership. *See Brandon Ridge*, 2007 WL 2209129 at *8. The court reiterates its prior holding that the 1997 amendments to § 6501(a) were only intended to clarify when the statute of limitations begins to run. (*See* Order Den. Mots. for J. on the Pleadings, No. 7:06-cv-181 (DE # 38) at 9.) The case law regarding which tax returns are available for review has not been disturbed.

The two other courts which have addressed this issue similarly have concluded that the court should consider the individual tax returns at issue as well as the partnership returns, where necessary. *See Salman Ranch*, 79 Fed. Cl. at 202-03 (holding that the court would review both the individual and partnership returns to determine whether adequate disclosure was present); *Brandon Ridge*, 2007 WL 2209129 at *8-9 (holding that in cases where there are references in the taxpayer's return to income from a pass-through entity, the returns from the pass-through entity also can be considered). When the court considers plaintiffs' disclosures, it may

review both information contained in plaintiffs' individual returns and in the partnership return, as necessary to determine whether plaintiffs adequately disclosed any amount in question.

As to the question of what is the proper standard to use in determining whether disclosures are adequate for purposes of § 6501(e)(1)(A)(ii), the parties's briefing is more extensive. Plaintiffs argue that *Colony* controls the inquiry. There the Court stated "[w]e think that in enacting § 275(c) Congress manifested no broader purpose than to give the Commissioner an additional two years to investigate tax returns in cases where, because of a taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors. In such instances the return on its face provides no clue to the existence of the omitted item." *Colony*, 357 U.S. at 36, 78 S. Ct. 1033.

As the court in *CC & F* found, several courts have continued to use the "clue" language from *Colony*. *CC & F Western Operations, Ltd.*, 273 F.3d at 407; *see also, White v. C.I.R.*, 991 F.2d 657, 661-62 (10th Cir. 1993) (citing *Colony* for the proposition that adequate disclosure requires returns to provide a "clue"); *Bishop v. United States*, 338 F. Supp. 1336, 1351 (N.D. Miss. 1970) (also citing *Colony* for the "clue" language). Plaintiffs do not articulate broadly what standard of disclosure constitutes a "clue." Instead, they assert that if an overstated basis may result in an omission of income, then a basis step-up and related sale disclosed on the same return provide an adequate "clue" for the IRS and thus adequate disclosure under § 6501(e)(1)(A)(ii). (*See* Mem. in Supp. of Pls.' Mot. for Summ. J. at 18.) The government, on the other hand, cites to a competing line of

cases that apply a more stringent standard. Specifically, the government cites *CC & F Western Operations, Ltd.*, 273 F.3d at 407, *Phinney*, 392 F.2d at 685, and *In re G-I Holdings*, 2006 WL 2595264, for the proposition that something more than a clue is required by § 6501(e)(1)(A)(ii).

Plaintiffs' reliance on *Colony* as establishing the test for adequate disclosure under § 6501(e)(1)(A)(ii) is misplaced. As noted above, *Colony* dealt with the predecessor provision to § 6501(e). The code section before the Court in *Colony* (§ 275(c)) contained no safe harbor provision. To the degree that *Colony* may have established any "clue" test,[10] it established it for § 275(c). The Court did not determine the meaning of § 6501(e)(1)(A)(ii) because that statute was not before the Court in that case. Accordingly, any suggestion by the Court that a "clue" is all that is needed to invoke adequate disclosure would simply be dicta that does little to enlighten the appropriate standard for disclosure as it relates to § 6501.[11]

This court concludes, after careful consideration, that the plain language of § 6501(e)(1)(A)(ii) requires some-

---

[10] The First Circuit does not espouse even that *Colony* established such a test. As the court explained in *CC & F*, "[t]he only test adopted in Colony was that there be an omission of gross receipts exceeding 25 percent and not just an overstatement of basis that effectively reduced reportable gross income by that amount. The clue language was used merely to explain why Congress might have been more concerned about an omitted receipt than an overstated basis—specifically, because the omitted receipt will (ordinarily) provide no clue as to the error; by implicit contrast, an overstated basis provides something the IRS can check." *CC & F Western Operations, Ltd.*, 273 F.3d at 407.

[11] Even though the Court in *Colony* determined its holding to be in "harmony" with newly enacted § 6501(e), that harmony, as discussed *supra* does not come from subsection (ii) but rather from subsection (i).

thing "far more than a mere clue that might intrigue Sherlock Holmes." *CC & F Western Operations, Ltd.*, 273 F.3d at 407. This court, like the court in *CC & F*, finds that the language of this section requires the taxpayer's return provide more than a clue—it must disclose the nature and amount of the alleged omission from gross income where subsection (ii) explicitly requires that disclosure must be made "in a manner adequate to apprise the Secretary of the nature and amount of" any item omitted from gross income. 26 U.S.C. § 6501(e)(1)(A)(ii). This language indicates that Congress wanted more than a "clue" as to the omitted amount's existence before a taxpayer should be allowed to invoke safe harbor protection. The disclosure must be sufficient to indicate what type of item has been omitted and how large (or small) that item is on the face of the relevant returns. This does not mean that a taxpayer need include "a detailed disclosure of every precise fact that may underlie a transaction." *Salman Ranch*, 79 Fed. Cl. at 203. Rather, it means that the taxpayer must disclose the substance of a transaction in order to benefit from the shorter limitations period if the taxpayer omits income. *Id.* (citing *CC & F Western Operations, Ltd.*, 273 F.3d at 408).

The question whether an overstatement of basis can constitute an omission is, therefore, answered in the affirmative. Further, the court may, at the appropriate time, consider both the partnership and individual taxpayers' income tax returns in determining adequate disclosure under § 6501(e)(1)(A)(ii). And, the court will apply a disclosure standard that requires that the nature and amount of any potentially omitted amounts be disclosed on the face of those returns to qualify for the safe harbor provision. The court holds in abeyance decision

on the remaining issues presented bearing on applicability of the extended limitations period pending supplemental briefing expressly on: 1) whether plaintiffs overstated basis; and, if so, 2) can the court, on the record before it, now determine whether the resulting omission from gross income was or was not in excess of 25 percent of the stated gross income amount; and, if it was 3) whether the safe harbor of § 6501(e)(1)(A)(ii) applies here. These issues shall be the subject of the parties' supplemental briefing, in light of the decisions herein rendered, so that the court may more fully consider them. The parties' supplemental memoranda, not to exceed 30 pages in length, shall be filed and served on or before December 22, 2008. Responses, not to exceed 15 pages in length, shall be filed and served on or before January 19, 2009.

CONCLUSION

For the reasons given, plaintiff's motion for summary judgment is denied in part, and in corresponding part, defendant's motion is allowed. The court holds in abeyance decision on remaining parts pending receipt and review of supplemental briefing herein ordered.

APPENDIX D

1. 26 U.S.C. 275 (1934) provides:

Period of limitation upon assessment and collection. Except as provided in section 276—

(a) General rule. The amount of income taxes imposed by this chapter shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

(b) Request for prompt assessment. In the case of income received during the lifetime of a decedent, or by his estate during the period of administration, or by a corporation, the tax shall be assessed, and any proceeding in court without assessment for the collection of such tax shall be begun, within eighteen months after written request therefor (filed after the return is made) by the executor, administrator, or other fiduciary representing the estate of such decedent, or by the corporation, but not after the expiration of three years after the return was tiled. This subsection shall not apply in the case of a corporation unless—

(1) Such written request notifies the Commissioner that the corporation contemplates dissolution at or before the expiration of such 18 months' period; and

(2) The dissolution is in good faith begun before the expiration of such 18 months' period; and

(3) The dissolution is completed.

(c) Omission from gross income. If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may

be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

(d) **Return filed before last day.** For the purposes of subsections (a), (b), and (c), a return filed before the last day prescribed by law for the filing thereof shall be considered as filed on such last day.

(e) **Corporation and shareholder.** If a corporation makes no return of the tax imposed by this chapter, but each of the shareholders includes in his return his distributive share of the net income of the corporation, then the tax of the corporation shall be assessed within four years after the last date on which any such shareholder's return was filed. (May 10, 1934, 11:40 a.m., c. 277, § 275, 48 Stat. 745.)

2. 26 U.S.C. 6229(c)(2) (2000) provides:

Period of limitations for making assessments

(c) Special rule in case of fraud, etc.

(2) Substantial omission of income

If any partnership omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in its return, subsection (a) shall be applied by substituting "6 years" for "3 years".

3. 26 U.S.C. 6501(e)(1)(A) (1954) provides:

Limitations on assessment and collection.

(e) Omission from gross income.

Except as otherwise provided in subsection (c)—

(1) Income taxes.

In the case of any tax imposed by subtitle A—

(A) General rule.

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item.

4. 26 U.S.C. 6501(e)(1)(A) (2000) provides:

Limitations on assessment and collection

(e) Substantial omission of items

Except as otherwise provided in subsection (c)—

(1) Income taxes

In the case of any tax imposed by subtitle A—

(A) General rule

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item.

5. 26 C.F.R. 301.6229(c)(2)-1 provides:

Substantial omission of income.

(a) *Partnership return*—(1) *General rule.* (i) If any partnership omits from the gross income stated in its return an amount properly includible therein and that amount is described in clause (i) of section 6501(e)(1)(A), subsection (a) of section 6229 shall be applied by substituting "6 years" for "3 years."

(ii) For purposes of paragraph (a)(1)(i) of this section, the term gross income, as it relates to a trade or business, means the total of the amounts received or accrued from the sale of goods or services, to the extent required to be shown on the return, without reduction for the cost of those goods or services.

(iii) For purposes of paragraph (a)(1)(i) of this section, the term gross income, as it relates to any income other than from the sale of goods or services in a trade or business, has the same meaning as provided under section 61(a), and includes the total of the amounts received or accrued, to the extent required to be shown on the return. In the case of amounts received or accrued that relate to the disposition of property, and except as provided in paragraph (a)(1)(ii) of this section, gross income means the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property. Consequently, except as provided in paragraph (a)(1)(ii) of this section, an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6229(c)(2).

(iv) An amount shall not be considered as omitted from gross income if information sufficient to apprise the Commissioner of the nature and amount of the item is disclosed in the return, including any schedule or statement attached to the return.

(b) *Effective/applicability date.* The rules of this section apply to taxable years with respect to which the applicable period for assessing tax did not expire before September 24, 2009.

(c) *Expiration date.* The applicability of this section expires on or before September 24, 2012.

6. 26 C.F.R. 301.6501(e)-1 provides:

Omission from return.

(a) *Income taxes*—(1) *General rule.* (i) If a taxpayer omits from the gross income stated in the return of a tax imposed by subtitle A of the Internal Revenue Code an amount properly includible therein that is in excess of 25 percent of the gross income so stated, the tax may be assessed, or a proceeding in court for the collection of that tax may be begun without assessment, at any time within 6 years after the return was filed.

(ii) For purposes of paragraph (a)(1)(i) of this section, the term gross income, as it relates to a trade or business, means the total of the amounts received or accrued from the sale of goods or services, to the extent required to be shown on the return, without reduction for the cost of those goods or services.

(iii) For purposes of paragraph (a)(1)(i) of this section, the term gross income, as it relates to any income

other than from the sale of goods or services in a trade or business, has the same meaning as provided under section 61(a), and includes the total of the amounts received or accrued, to the extent required to be shown on the return. In the case of amounts received or accrued that relate to the disposition of property, and except as provided in paragraph (a)(1)(ii) of this section, gross income means the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property. Consequently, except as provided in paragraph (a)(1)(ii) of this section, an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A)(i).

(iv) An amount shall not be considered as omitted from gross income if information sufficient to apprise the Commissioner of the nature and amount of the item is disclosed in the return, including any schedule or statement attached to the return.

(2) [Reserved]

(b) *Effective/applicability date.* Estate and gift taxes—(1) If the taxpayer omits from the gross estate as stated in the estate tax return, or from the total amount of the gifts made during the period for which the gift tax return was filed (see § 25.6019-1 of this chapter) as stated in the gift tax return, an item or items properly includible therein the amount of which is in excess of 25 percent of the gross estate as stated in the estate tax return, or 25 percent of the total amount of the gifts as stated in the gift tax return, the tax may be assessed, or a proceeding in court for the collection thereof may be

begun without assessment, at any time within 6 years after the estate tax or gift tax return, as applicable, was filed.

(2) For purposes of this paragraph (b), an item disclosed in the return or in any schedule or statement attached to the return in a manner sufficient to apprise the Commissioner of the nature and amount thereof shall not be taken into account in determining items omitted from the gross estate or total gifts, as the case may be. Further, there shall not be taken into account in computing the 25 percent omission from the gross estate stated in the estate tax return or from the total gifts stated in the gift tax return, any increases in the valuation of assets disclosed on the return.

(c) *Excise taxes—(1) In general.* If the taxpayer omits from a return of a tax imposed under a provision of subtitle D an amount properly includible thereon, which amount is in excess of 25 percent of the amount of tax reported thereon, the tax may be assessed or a proceeding in court for the collection thereof may be begun without assessment, at any time within 6 years after the return was filed. For special rules relating to chapter 41, 42, 43 and 44 taxes, see paragraphs (c)(2), (3), (4), and (5) of this section.

(2) *Chapter 41 excise taxes.* If an organization discloses an expenditure in its return (or in a schedule or statement attached thereto) in a manner sufficient to apprise the Commissioner of the existence and nature of the expenditure, the three-year limitation on assessment and collection described in section 6501(a) shall apply with respect to any tax under chapter 41 arising from the expenditure. If a taxpayer fails to so disclose an expenditure in its return (or in a schedule or statement

attached thereto), the tax arising from the expenditure not so disclosed may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed.

(3) *Chapter 42 excise taxes.* (i) If a private foundation omits from its annual return with respect to the tax imposed by section 4940 an amount of tax properly includible therein that is in excess of 25 percent of the amount of tax imposed by section 4940 that is reported on the return, the tax may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed. If a private foundation discloses in its return (or in a schedule or statement attached thereto) the nature, source, and amount of any income giving rise to any omitted tax, the tax arising from the income shall be counted as reported on the return in computing whether the foundation has omitted more than 25 percent of the tax reported on its return.

(ii) If a private foundation, trust, or other organization (as the case may be) discloses an item in its return (or in a schedule or statement attached thereto) in a manner sufficient to apprise the Commissioner of the existence and nature of the item, the three-year limitation on assessment and collection described in section 6501(a) shall apply with respect to any tax imposed under sections 4941(a), 4942(a), 4943(a), 4944(a), 4945(a), 4951(a), 4952(a), 4953 and 4958, arising from any transaction disclosed by the item. If a private foundation, trust, or other organization (as the case may be) fails to so disclose an item in its return (or in a schedule or statement attached thereto), the tax arising from any

transaction not so disclosed may be assessed or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed.

(4) *Chapter 43 excise taxes.* If a taxpayer discloses an item in its return (or in a schedule or statement attached thereto) in a manner sufficient to apprise the Commissioner of the existence and nature of the item, the three-year limitation on assessment and collection described in section 6501(a) shall apply with respect to any tax imposed under sections 4971(a), 4972, 4973, 4974 and 4975(a), arising from any transaction disclosed by the item. If a taxpayer fails to so disclose an item in its return (or in a schedule or statement attached thereto), the tax arising from any transaction not so disclosed may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed. The applicable return for the tax under sections 4971, 4972, 4973 and 4974, is the return designated by the Commissioner for reporting the respective tax. The applicable return for the tax under section 4975 is the return filed by the plan used to report the act giving rise to the tax.

(5) *Chapter 44 excise taxes.* If a real estate investment trust omits from its annual return with respect to the tax imposed by section 4981 an amount of tax properly includible therein that is in excess of 25 percent of the amount of tax imposed by section 4981 that is reported on the return, the tax may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed. If a real estate investment trust discloses in its return (or in a schedule or statement at-

tached thereto) the nature, source, and amount of any income giving rise to any omitted tax, the tax arising from the income shall be counted as reported on the return in computing whether the trust has omitted more than 25 percent of the tax reported on its return.

(d) *Exception.* The provisions of this section do not limit the application of section 6501©.

(e) *Effective/applicability date—(1) Income taxes.* Paragraph (a) of this section applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009.

(2) *Estate, gift and excise taxes.* Paragraphs (b) through (d) of this section continue to apply as they did prior to being removed inadvertently on September 28, 2009. Specifically, paragraph (b) of this section applies to returns filed on or after May 2, 1956, except for the amendment to paragraph (b)(1) of this section that applies to returns filed on or after December 29, 1972. Paragraph (c) of this section applies to returns filed on or after October 7, 1982, except for the amendment to paragraph (c)(3)(ii) of this section that applies to returns filed on or after January 10, 2001. Paragraph (d) of this section applies to returns filed on or after May 2, 1956.

7. 75 Federal Register 78,897 provides:

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 301

[TD 9511]

RIN 1545-BI44

Definition of Omission From Gross Income

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations defining an omission from gross income for purposes of the six-year minimum period for assessment of tax attributable to partnership items and the six-year period for assessing tax. The regulations resolve a continuing issue as to whether an overstatement of basis in a sold asset results in an omission from gross income. The regulations will affect any taxpayer who overstates basis in a sold asset creating an omission from gross income exceeding twenty-five percent of the income stated in the return. Additionally, provisions related to estate, gift and excise tax are reinstated from the prior final regulation.

DATES: *Effective Date*: These regulations are effective on December 14, 2010.

Applicability Date: The regulations relating to income taxes apply to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009, which is the date that the proposed and temporary regulations to which these regulations relate were filed with the **Federal Register**. For dates of applicability regarding the regulations relating to estate, gift and excise taxes, see § 301.6501(e)-1(e)(2).

FOR FURTHER INFORMATION CONTACT: William A. Heard, III at (202) 622-4570 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Procedure and Administration Regulations (26 CFR part 301) under section 6229(c)(2) and section 6501(e) of the Internal Revenue Code. On September 28, 2009, temporary regulations (TD 9466) regarding the definition of an omission from gross income for purposes of the six-year period for assessment were published in the **Federal Register** (74 FR 49321). A notice of proposed rulemaking (REG-108045-08) cross-referencing the temporary regulations was published in the **Federal Register** for the same day (74 FR 49354). One written comment was received from the public in response to the notice of proposed rulemaking. No public hearing was requested or held. After consideration of the comment, the proposed regulations are adopted as amended by this Treasury decision, and the corresponding temporary regulations are removed.

Summary of Comments and Explanation of Revisions

These final regulations amend the Procedure and Administration Regulations (26 CFR part 301) relating to sections 6229(c)(2) and 6501(e). In addition to the revisions set forth in the proposed regulations cross-referencing the temporary regulations, the final regulations reflect structural amendments to sections 6229(c)(2) and 6501(e) in the Hiring Incentives To Restore Employment Act (Pub. L. 111-147, 124 Stat. 112) to accommodate an additional threshold triggering the six-year period of limitations for omissions from gross income attributable to assets subject to certain reporting requirements, which is not otherwise addressed in these final regulations. The final regulations also clarify the effective/applicability date provisions in the section

6229(c)(2) and section 6501(e) regulations to eliminate a perceived ambiguity in the temporary regulations, that was brought to light by the Tax Court in *Intermountain Insurance Service of Vail v. Commissioner*, 134 T.C. No. 11 (2010), appeal docketed, No. 10-1204 (DC Cir.).

As explained in the preamble to the temporary regulations, the United States Courts of Appeals for the Ninth Circuit and the Federal Circuit construed section 6501(e)(1) in cases outside the trade-or-business context contrary to the interpretation provided in these final regulations, holding that an overstatement of basis does not constitute an "omission." *Bakersfield Energy Partners v. Commissioner*, 568 F.3d 767 (9th Cir. 2009); *Salman Ranch Ltd v. United States*, 573 F.3d 1362 (Fed. Cir. 2009). Those courts relied on the Supreme Court's opinion in *Colony v. Commissioner*, 357 U.S. 28 (1958), which dealt with an omission from gross income in the context of a trade or business under the predecessor of section 6501(e). The Treasury Department and the Internal Revenue Service disagree with those courts that the Supreme Court's reading of the predecessor to section 6501(e) in *Colony* applies to sections 6501(e)(1) and 6229(c)(2), for the reasons set forth in the preamble to the temporary regulations.

After publication of the temporary regulations, the Tax Court declared the temporary regulations invalid, adhering to its prior opinion in *Bakersfield Energy Partners v. Commissioner*, 128 T.C. 207 (2007). *Intermountain Insurance Service of Vail v. Commissioner*, 134 T.C. No. 11 (2010), appeal docketed, No. 10-1204 (DC Cir.). In part, the Tax Court in *Intermountain* concluded that the Supreme Court's opinion in Colony was the only permissible interpretation of the statutory lan-

guage in question ("omits from gross income"). The Treasury Department and the Internal Revenue Service disagree with *Intermountain*. The Supreme Court stated in *Colony* that the statutory phrase "omits from gross income" is ambiguous, meaning that it is susceptible to more than one reasonable interpretation. The interpretation adopted by the Supreme Court in *Colony* represented that court's interpretation of the phrase but not the only permissible interpretation of it. Under the authority of *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 982-83 (2005), the Treasury Department and the Internal Revenue Service are permitted to adopt another reasonable interpretation of "omits from gross income," particularly as it is used in a new statutory setting. *See Hernandez-Carrera v. Carlson*, 547 F.3d 1237 (10th Cir. 2008) (agencies are free to promulgate a reasonable construction of an ambiguous statute that contradicts any court's interpretation, even the Supreme Court's). The interpretation of the phrase "omits from gross income" as used in section 6501(e)(1) is currently pending before several United States Courts of Appeals.

Because these regulations are a clarification of the period of limitations provided in sections 6501(e)(1) and 6229(c)(2) and are consistent with the Secretary's application of those provisions both with respect to a trade or business (that is, gross income means gross receipts), as well as outside of the trade-or-business context (that is, the section 61 definition of gross income applies), they are applicable to all cases with respect to which the period for assessing tax was open on or after September 24, 2009, the date the temporary regulations were filed with the **Federal Register**.

1. Retroactivity

The sole written comment received in response to the notice of proposed rulemaking by cross-reference to the temporary regulations questioned the application of the regulations, characterizing them as retroactive, and recommended that they be applied only prospectively. The commentator stated that the temporary regulations apply with retroactive effect "in that taxable years which had closed are now reopened." The Treasury Department and the Internal Revenue Service disagree with the characterization of the regulations as retroactive. The final regulations have been clarified to emphasize that they only apply to open tax years, and do not reopen closed tax years as suggested by the commentator.

The commentator also relied on the 1996 amendments to section 7805(b) to argue that retroactively effective Treasury regulations are impermissible, with limited exceptions. The 1996 amendments to section 7805(b), however, do not apply to the regulations under sections 6229(c)(2) and 6501(e)(1). That is because those amendments are only effective for regulations that relate to statutory provisions enacted on or after July 30, 1996. Taxpayer Bill of Rights 2 (Pub. L. 104-168, section 1101(a), 110 Stat. 1469). Since section 6229(c)(2) was enacted in 1982 and section 6501(e)(1)(A) was enacted in 1954 (and redesignated as subparagraph (B) as part of the HIRE Act in 2010), the 1996 amendments to section 7805(b) are inapplicable to the regulations. Prior to the 1996 amendments, section 7805(b) provided, "The Secretary may prescribe the extent, if any, to which any ruling or regulation, relating to the internal revenue laws, shall be applied without retroactive effect." Although these regulations are not retroactive, a retroactive regu-

lation interpreting sections 6229(c)(2) and 6501(e)(1) is expressly permitted by the applicable version of section 7805(b), which presumes regulations to apply retroactively unless otherwise provided.

2. Intermountain

The Tax Court's majority in *Intermountain* erroneously interpreted the applicability provisions of the temporary and proposed regulations, which provided that the regulations applied to taxable years with respect to which "the applicable period for assessing tax did not expire before September 24, 2009." The Internal Revenue Service will continue to adhere to the position that "the applicable period" of limitations is not the "general" three-year limitations period. The three-year limitations period is one of several limitations periods in the Internal Revenue Code, including the six-year limitations period under sections 6229(c)(2) and 6501(e)(1). The expiration of the three-year period does not "close" a taxable year if a longer period applies. Consistent with that position, the final regulations apply to taxable years with respect to which the six-year period for assessing tax under section 6229(c)(2) or 6501(e)(1) was open on or after September 24, 2009. This includes, but is not limited to, all taxable years (1) for which six years had not elapsed from the later of the date that a tax return was due or actually filed, (2) that are the subject of any case pending before any court of competent jurisdiction (including the United States Tax Court and Court of Federal Claims) in which a decision had not become final (within the meaning of section 7481) or (3) with respect to which the liability at issue had not become fixed pursuant to a closing agreement entered into under section 7121. The Internal Revenue Service's posi-

tion is consistent with the effective/applicability date provisions of these final regulations.

3. Other Revisions

The final regulations are amended to reinstate estate, gift and excise tax provisions that were inadvertently removed by the temporary regulations.

Special Analyses

It has been determined that these regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, the NPRM cross-referencing the temporary regulations preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Drafting Information

The principal author of these regulations is William A. Heard III of the Office of the Associate Chief Counsel (Procedure and Administration).

List of Subjects in 26 CFR Part 301

Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Penalties, Reporting and record-keeping requirements.

Adoption of Amendments to the Regulations

■ Accordingly, 26 CFR part 301 is amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

■ **Paragraph 1.** The authority citation for part 301 is amended by adding an entry in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Section 301.6229(c)(2)-1 is also issued under 26 U.S.C. 6230(k). * * *

■ **Par. 2.** Section 301.6229(c)(2)-1 is added to read as follows:

§ 301.6229(c)(2)-1 Substantial omission of income.

(a) *Partnership return*—(1) *General rule.* (i) If any partnership omits from the gross income stated in its return an amount properly includible therein and that amount is described in clause (i) of section 6501(e)(1)(A), subsection (a) of section 6229 shall be applied by substituting "6 years" for "3 years."

(ii) For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to a trade or business, means the total of the amounts received or accrued from the sale of goods or services, to the extent required to be shown on the return, without reduction for the cost of those goods or services.

(iii) For purposes of paragraph (a)(1)(i) of this section, the term gross income, as it relates to any income other than from the sale of goods or services in a trade or business, has the same meaning as provided under section 61(a), and includes the total of the amounts received or accrued, to the extent required to be shown on the return. In the case of amounts received or accrued that relate to the disposition of property, and except as provided in paragraph (a)(1)(ii) of this section, gross income means the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property. Consequently, except as provided in paragraph (a)(1)(ii) of this section, an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6229(c)(2).

(iv) An amount shall not be considered as omitted from gross income if information sufficient to apprise the Commissioner of the nature and amount of the item is disclosed in the return, including any schedule or statement attached to the return.

(b) *Effective/applicability date.* This section applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009.

§ 301.6229(c)(2)-1T [Removed]

■ Par. 3. Section 6229(c)(2)-1T is removed.

■ Par. 4. Section 301.6501(e)-1 is added to read as follows:

§ 301.6501(e)-1 Omission from return.

(a) *Income taxes*—(1) *General rule.* (i) If a taxpayer omits from the gross income stated in the return of a tax imposed by subtitle A of the Internal Revenue Code an amount properly includible therein that is in excess of 25 percent of the gross income so stated, the tax may be assessed, or a proceeding in court for the collection of that tax may be begun without assessment, at any time within 6 years after the return was filed.

(ii) For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to a trade or business, means the total of the amounts received or accrued from the sale of goods or services, to the extent required to be shown on the return, without reduction for the cost of those goods or services.

(iii) For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to any income other than from the sale of goods or services in a trade or business, has the same meaning as provided under section 61(a), and includes the total of the amounts received or accrued, to the extent required to be shown on the return. In the case of amounts received or accrued that relate to the disposition of property, and except as provided in paragraph (a)(1)(ii) of this section, *gross income* means the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property. Consequently, except as provided in paragraph (a)(1)(ii) of this section, an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A)(i).

(iv) An amount shall not be considered as omitted from gross income if information sufficient to apprise the Commissioner of the nature and amount of the item is disclosed in the return, including any schedule or statement attached to the return.

(2) [Reserved]

(b) *Estate and gift taxes*—(1) If the taxpayer omits from the gross estate as stated in the estate tax return, or from the total amount of the gifts made during the period for which the gift tax return was filed (see § 25.6019-1 of this chapter) as stated in the gift tax return, an item or items properly includible therein the amount of which is in excess of 25 percent of the gross estate as stated in the estate tax return, or 25 percent of the total amount of the gifts as stated in the gift tax return, the tax may be assessed, or a proceeding in court for the collection thereof may be begun without assessment, at any time within 6 years after the estate tax or gift tax return, as applicable, was filed.

(2) For purposes of this paragraph (b), an item disclosed in the return or in any schedule or statement attached to the return in a manner sufficient to apprise the Commissioner of the nature and amount thereof shall not be taken into account in determining items omitted from the gross estate or total gifts, as the case may be. Further, there shall not be taken into account in computing the 25 percent omission from the gross estate stated in the estate tax return or from the total gifts stated in the gift tax return, any increases in the valuation of assets disclosed on the return.

(c) *Excise taxes*—(1) *In general.* If the taxpayer omits from a return of a tax imposed under a provision

of subtitle D an amount properly includible thereon, which amount is in excess of 25 percent of the amount of tax reported thereon, the tax may be assessed or a proceeding in court for the collection thereof may be begun without assessment, at any time within 6 years after the return was filed. For special rules relating to chapter 41, 42, 43 and 44 taxes, see paragraphs (c)(2), (3), (4), and (5) of this section.

(2) *Chapter 41 excise taxes.* If an organization discloses an expenditure in its return (or in a schedule or statement attached thereto) in a manner sufficient to apprise the Commissioner of the existence and nature of the expenditure, the three-year limitation on assessment and collection described in section 6501(a) shall apply with respect to any tax under chapter 41 arising from the expenditure. If a taxpayer fails to so disclose an expenditure in its return (or in a schedule or statement attached thereto), the tax arising from the expenditure not so disclosed may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed.

(3) *Chapter 42 excise taxes.* (i) If a private foundation omits from its annual return with respect to the tax imposed by section 4940 an amount of tax properly includible therein that is in excess of 25 percent of the amount of tax imposed by section 4940 that is reported on the return, the tax may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed. If a private foundation discloses in its return (or in a schedule or statement attached thereto) the nature, source, and amount of any income giving rise

to any omitted tax, the tax arising from the income shall be counted as reported on the return in computing whether the foundation has omitted more than 25 percent of the tax reported on its return.

(ii) If a private foundation, trust, or other organization (as the case may be) discloses an item in its return (or in a schedule or statement attached thereto) in a manner sufficient to apprise the Commissioner of the existence and nature of the item, the three-year limitation on assessment and collection described in section 6501(a) shall apply with respect to any tax imposed under sections 4941(a), 4942(a), 4943(a), 4944(a), 4945(a), 4951(a), 4952(a), 4953 and 4958, arising from any transaction disclosed by the item. If a private foundation, trust, or other organization (as the case may be) fails to so disclose an item in its return (or in a schedule or statement attached thereto), the tax arising from any transaction not so disclosed may be assessed or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed.

(4) *Chapter 43 excise taxes.* If a taxpayer discloses an item in its return (or in a schedule or statement attached thereto) in a manner sufficient to apprise the Commissioner of the existence and nature of the item, the three-year limitation on assessment and collection described in section 6501(a) shall apply with respect to any tax imposed under sections 4971(a), 4972, 4973, 4974 and 4975(a), arising from any transaction disclosed by the item. If a taxpayer fails to so disclose an item in its return (or in a schedule or statement attached thereto), the tax arising from any transaction not so disclosed may be assessed, or a proceeding in court for the collec-

tion of the tax may be begun without assessment, at any time within 6 years after the return was filed. The applicable return for the tax under sections 4971, 4972, 4973 and 4974, is the return designated by the Commissioner for reporting the respective tax. The applicable return for the tax under section 4975 is the return filed by the plan used to report the act giving rise to the tax.

(5) *Chapter 44 excise taxes.* If a real estate investment trust omits from its annual return with respect to the tax imposed by section 4981 an amount of tax properly includible therein that is in excess of 25 percent of the amount of tax imposed by section 4981 that is reported on the return, the tax may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time within 6 years after the return was filed. If a real estate investment trust discloses in its return (or in a schedule or statement attached thereto) the nature, source, and amount of any income giving rise to any omitted tax, the tax arising from the income shall be counted as reported on the return in computing whether the trust has omitted more than 25 percent of the tax reported on its return.

(d) *Exception.* The provisions of this section do not limit the application of section 6501(c).

(e) *Effective/applicability date*—(1) *Income taxes.* Paragraph (a) of this section applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009.

(2) *Estate, gift and excise taxes.* Paragraphs (b) through (d) of this section continue to apply as they did prior to being removed inadvertently on September 28, 2009. Specifically, paragraph (b) of this section applies

to returns filed on or after May 2, 1956, except for the amendment to paragraph (b)(1) of this section that applies to returns filed on or after December 29, 1972. Paragraph (c) of this section applies to returns filed on or after October 7, 1982, except for the amendment to paragraph (c)(3)(ii) of this section that applies to returns filed on or after January 10, 2001. Paragraph (d) of this section applies to returns filed on or after May 2, 1956.

OPPOSITION BRIEF

No. 11-139

In The
Supreme Court of the United States

UNITED STATES OF AMERICA,

Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, *et al.*,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Richard T. Rice
Counsel of Record
Charles M. Wiley
Michael R. Cashin
Robert T. Numbers, II
WOMBLE CARLYLE SANDRIDGE & RICE, PLLC
One West 4th Street
Winston-Salem, North Carolina 27101
(336) 721-3609
rrice@wcsr.com

Counsel for Respondents

Dated: August 26, 2011

THE LEX GROUP DC • 1825 K Street, N.W. • Suite 103 • Washington, D.C. 20006
(202) 955-0001 • (800) 856-4419 • Fax (202) 955-0022 • www.thelexgroup.com

QUESTIONS PRESENTED

1. Whether this case rises to the level of importance worthy of the Supreme Court's consideration in light of the enactment of 26 U.S.C. § 6501(c)(10) (2004) by Congress.

2. Whether an understatement of income resulting from an overstatement of the tax basis of sold property can qualify as an omission from gross income for purposes of the extended, six-year assessment period set forth in 26 U.S.C. § 6501(e)(1)(A) (1999).

3. Whether a final regulation promulgated by the Department of Treasury during the appeal of this case in direct conflict with Supreme Court precedent in *Colony, Inc. v. Commissioner*, 357 U.S. 28 (1958), is entitled to deference by the Supreme Court.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Supreme Court Rules of Procedure, taxpayers state that there is no parent corporation or publicly held corporation that owns 10% or more of the stock of any of the corporate taxpayers.

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED i

CORPORATE DISCLOSURE STATEMENT ii

TABLE OF CONTENTS iii

TABLE OF AUTHORITIES v

STATEMENT OF THE CASE 1

REASONS FOR DENYING WRIT 4

I. Congress addressed petitioner's concerns when it enacted 26 U.S.C. § 6501(c)(10) 4

II. This Court's decision in *Colony* controls the statute of limitations period in this case 8

A. Colony is not limited to cases involving the sale of goods or services in a trade or business 10

B. The gross receipts and adequate disclosure provisions are not superfluous 20

III. The Regulation is inapplicable to this case 24

A. The Regulation does not apply by its own terms, is an abuse of executive power and violates due process 24

B. The Regulation does not deserve *Chevron* deference 28

C. *Brand X* does not control 30

CONCLUSION 33

TABLE OF AUTHORITIES

Page(s)

CASES

Bakersfield Energy Partners, LP v. Comm'r,
568 F.3d 767 (9th Cir. 2009) 9, 24, 25

Beard v. Comm'r,
633 F.3d 616 (7th Cir. 2011),
petition for cert. filed,
80 U.S.L.W. 3004
(U.S. June 23, 2011) (No. 10-1553).....7, 9, 21

Burks v. United States,
633 F.3d 347 (5th Cir. 2011),
petition for cert. filed,
80 U.S.L.W. 3090
(U.S. Aug. 11, 2011) (No. 11-178) 7, 9

Chevron, U.S.A., Inc. v.
Natural Res. Def. Council, Inc.,
467 U.S. 837 (1984) .....*passim*

Chock Full O'Nuts Corp. v. United States,
453 F.2d 300 (2d Cir. 1971).....26, 27

Colony, Inc. v. Comm'r,
244 F.2d 75 (6th Cir. 1957) 14

Colony, Inc. v. Comm'r,
357 U.S. 28 (1958) .....*passim*

Comm'r v. Goodwyn Crockery Co.,
315 F.2d 110 (6th Cir. 1963) 26

Davis v. Hightower,
230 F.2d 549 (5th Cir. 1956) ... 13-14, 18, 22, 23

Ewald v. Comm'r,
141 F.2d 750 (6th Cir. 1944) 11

Gen. Dynamics Land Sys., Inc. v. Cline,
540 U.S. 581 (2004) 29

Goodenow v. Comm'r,
238 F.2d 20 (8th Cir. 1956) 14, 18

Grapevine Imports, Ltd. v. United States,
636 F.3d 1368 (Fed. Cir. 2011),
petition for cert. filed,
80 U.S.L.W. 3090
(U.S. Aug. 5, 2011) (No. 11-163) 7, 9

Helvering v. R.J. Reynolds Tobacco Co.,
306 U.S. 110 (1939) 26

Home Concrete & Supply, LLC v. United States,
634 F.3d 249 (4th Cir. 2011) ..... *passim*

Homes by Ayres v. Comm'r,
795 F.2d 832 (9th Cir. 1986) 17

Intermountain Ins. Servs. of Vail, LLC v. Comm'r,
--- F.3d ---, 2011 WL 2451011
(D.C.Cir. 2011) 7, 9, 21

Int'l Bus. Machs. Corp. v. United States,
343 F.2d 914 (Ct. Cl. 1965) 26

Lesavoy Found. v. Comm'r,
238 F.2d 589 (3d Cir. 1956) 26-27

Mayo Found. For Med. Educ. & Research v. United States,
562 U.S. ___ (2011) 32

Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.,
545 U.S. 967 (2005) 30, 31, 32

Reis v. Comm'r,
142 F.2d 900 (6th Cir. 1944) 11, 14

Rice v. Sioux City Mem'l Park Cemetery,
349 U.S. 70 (1955) 8

Salman Ranch, Ltd. v. Comm'r,
--- F.3d ---, 2011 WL 2120044
(10th Cir. 2011) 7, 9

Salman Ranch, Ltd. v. United States,
573 F.3d 1362 (Fed. Cir. 2009) ..... *passim*

Slaff v. Comm'r,
220 F.2d 65 (9th Cir. 1955) 13, 18

Sutherland Lumber-Southwest, Inc. v. Comm'r,
114 T.C. 197 (2000), *aff'd per curiam*,
255 F.3d 495 (8th Cir. 2001) 6-7

Uptegrove Lumber Co. v. Comm'r,
204 F.2d 570 (3d Cir. 1953)..... *passim*

United States v. Carlton,
512 U.S. 26 (1994) 28

W.C. & A.N. Miller Dev. Co. v. Comm'r,
81 T.C. 619 (1983) 17

Wilmington Partners L.P., et al. v. Comm'r,
Tax Court Docket No. 15098-06,
appeal filed No. 10-4183
(2d Cir. filed Oct. 13, 2010) 25

Woodward v. United States,
322 F. Supp. 332 (W.D.Va. 1971)..... 27

Zuni Pub. Sch. Dist. No. 89 v. Dep't. of Educ.,
550 U.S. 81 (2007) 29

CONSTITUTIONAL PROVISION

U.S. CONST. amend. V 28

STATUTES

26 U.S.C. § 22 (1939) 12, 13

26 U.S.C. § 61..... 12, 13, 20

26 U.S.C. § 274(e)(2)(B) 7

26 U.S.C. § 275(c) (1939) ..... *passim*

26 U.S.C. § 6011 5

26 U.S.C. § 6221 2

26 U.S.C. § 6223(a)(2) 2

26 U.S.C. § 6229(d) 2

26 U.S.C. § 6501(a) 2

26 U.S.C. § 6501(c)(10) ..... *passim*

26 U.S.C. § 6501(e) 6, 30

26 U.S.C. § 6501(e)(1)(A) ..... *passim*

26 U.S.C. § 6501(e)(1)(A)(i) 22

26 U.S.C. § 6501(e)(1)(A)(ii) 22

26 U.S.C. § 6707A(c)(2) 5

26 U.S.C. § 6112 5

26 U.S.C. § 6112(b) 5

REGULATIONS

Temp. Proc. and Admin. Reg. § 301.6111-2T(b)(2) 6

Temp. Treas. Reg. § 1.6011-4T(b)(2) 6

Temp. Treas. Reg. § 301.6501(e)-1T 3, 24

Treas. Reg. § 1.170A-13(f)(5) 18

Treas. Reg. § 1.61-3(a) 12

Treas. Reg. 111, 29.22(a)-5 9 (1939) 12

Treas. Reg. § 301.6501(e)-1 ..... 3, 24

Treas. Reg. § 301.6501(e)-1(e)(1) 25

OTHER AUTHORITIES

American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 413(c)(28) 6

American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 814(a) 4

Black Lung Benefits Revenue Act of 1977, Pub. L. No. 95-227, § 4(d)(4) 6

Black's Law Dictionary 701 (7th ed. 1999) 18

Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, § 1016(a)(14) 6

Excise, Estate, and Gift Tax Adjustment Act of 1970, Pub. L. No. 91-614, § 102(d)(8) 6

Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, § 810(b) 6

Hiring Incentives to Restore Employment Act of 2010, Pub. L. No. 111-147, § 513(a)(1) 6

IRS Notice 2000-44, 2000-36 I.R.B. 255 5

Patrick J. Smith, *Brand X and Omissions from Gross Income*, TAX ANALYSTS, 665 (Feb. 1, 2010) 32

Patrick J. Smith, *Omissions From Gross Income and 'Numerators and Denominators,'* SPECIAL REPORT TAX NOTES, 157 (July 11, 2011) 17, 18

Pub. L. No. 108-357, § 907 (2004) 7

Revenue Act of 1978, Pub. L. No. 95-600, § 701(t)(3)(A) 6

T.D. 9466 25

T.D. 9511 25

Tax Reform Act of 1969, Pub. L. No. 91-172, § 101(g)(3) 6

Tax Reform Act of 1976, Pub. L. No. 94-455, §§ 1307(d)(2)(F)(vi) and 1906(b)(13)(A) Pub. L. No. 108-357, § 907 (2004) 6

U.C.C. § 9-102(a)(44) 17

Webster's Third New Int'l Dictionary 978 (1969) 18

STATEMENT OF THE CASE

This case involves an attempt by the Internal Revenue Service ("IRS") to address a statute of limitations issue that has already been addressed by Congress and this Court. The petition for writ of certiorari should be denied for the reasons set forth herein.

Home Oil & Coal Company, Inc. ("Home Oil") was a small family business in Salisbury, NC that had been in operation for over 50 years before the transactions underlying this case took place. Robert Pierce worked for the family business part-time as a teenager before beginning work there fulltime in 1968. Steven Chandler began working there in 1972. Mr. Pierce and Mr. Chandler were the only two shareholders of Home Oil in 1999. Mr. Pierce owned approximately 81 percent, and Mr. Chandler owned approximately 19 percent of the outstanding shares at the time. The business evolved from selling home heating oil to primarily selling concrete for residential construction.

By early 1999, Mr. Pierce had decided he wanted to retire and sell the business. Given the importance of the sale for himself and his family, Mr. Pierce sought financial planning assistance from several highly recommended financial and legal professionals. Upon advice of those professionals, the taxpayers sold the business in 1999 and reported the sale in their tax returns which were timely filed in April 2000. Unfortunately, the advice of those professionals, and the transactions that took place

upon the sale of the family business, are what have lead to this litigation.

The family business was sold by a partnership that was formed on April 15, 1999, called Home Concrete & Supply, LLC ("Home Concrete"). For federal income tax purposes, the income tax treatment of partnership items is determined at the partnership level. 26 U.S.C. § 6221 (1999). If, on audit, the Internal Revenue Service ("IRS") determines that an adjustment should be made in an income tax return filed by a partnership, it issues a Federal Partnership Administrative Adjustment ("FPAA"). 26 U.S.C. § 6223(a)(2) (1999). The issuance of the FPAA stops the running of the applicable statute of limitations for the assessment of additional taxes. 26 U.S.C. § 6229(d) (1999).

Petitioner issued the FPAA to Home Concrete for its 1999 tax year on September 7, 2006, well beyond the three year period for assessing income tax specified in 26 U.S.C. § 6501(a) (1999). The FPAA proposed to reduce the reported basis in the assets of Home Concrete at the time of Home Concrete's sale of such assets in 1999. Home Concrete correctly reported on its income tax return the gross sales price from the sale of its assets, and disclosed an itemized increase in basis for each class of assets in the partnership, but petitioner asserts that Home Concrete overstated its basis in such assets in a transaction that it later labeled a "Son-of-BOSS" tax shelter.

Respondents filed their complaint in this action with the Eastern District of North Carolina on

December 5, 2006, seeking a declaration that the FPAA was barred by the three-year statute of limitations. In addition to declaratory relief, respondents sought the return of the $1,392,118.00 deposited with the trial court below, plus any accrued interest. Petitioner contended that the FPAA was timely because the six-year statute of limitations contained in § 6501(e)(1)(A) had not run, and the trial court agreed, entering partial summary judgment for petitioner on March 9, 2009.

On September 28, 2009, the Secretary of Treasury promulgated Temporary Treasury Regulation § 301.6501(e)-1T (2009) (the "Regulation"), in which the Treasury concludes that "an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A)." *Id.* The Secretary published the Regulation in final form without any material changes on December 17, 2010. Treas. Reg. § 301.6501(e)-1 (2010).

On February 7, 2011, after briefing and oral argument, the Court of Appeals for the Fourth Circuit reversed the trial court, concluding that this Court's decision in *Colony, Inc. v. Commissioner*, 357 U.S. 28 (1958), "forecloses the argument that Home Concrete's overstated basis in its reporting of the short sale proceeds resulted in an omission from its reported gross income." *Home Concrete & Supply, LLC v. U.S.*, 634 F.3d 249, 255 (4th Cir. 2011). The Court of Appeals also refused to apply the Regulation retroactively to this case because it was both inapplicable by its own terms and purported "to

establish a rule contrary to *Colony* to subject the taxpayers to the extended limitations period ten years later." *Id.* at 257. Petitioner filed a petition for rehearing en banc, which was denied in an order dated April 5, 2011. On August 3, 2011, petitioner filed a petition for writ of certiorari with this Court.

REASONS FOR DENYING WRIT

I. Congress addressed petitioner's concerns when it enacted 26 U.S.C. § 6501(c)(10).

The threshold question is whether the issue presented in this case, and other similar cases, is worthy of consideration by this Court. The answer is no.

Petitioner has labeled the transaction entered into by respondents in this case a "Son-of-BOSS" tax shelter,[1] which begs the question—What is the appropriate statute of limitations for assessing additional tax when a taxpayer engages in an alleged "Son-of-BOSS" tax shelter? That issue was answered definitively by Congress in 2004 when it enacted 26 U.S.C. § 6501(c)(10) (2004) as part of the American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 814(a) (the "2004 Act").[2] Section 6501(c)(10) provides as follows:

---

[1] For purposes of this brief only, respondents use the terms "tax shelter" and "listed transaction" interchangeably.

[2] Pursuant to the 2004 Act, § 6501(c)(10) is effective for tax years with respect to which the period for assessing a deficiency did not expire before October 22, 2004. Because, under *Colony*, respondents' statutes of limitations were closed before October 22, 2004, this provision is inapplicable to this case.

> (10) Listed transactions.—If a taxpayer fails to include on any return or statement for any taxable year any information with respect to a listed transaction (as defined in section 6707A(c)(2)) which is required under section 6011 to be included with such return or statement, the time for assessment of any tax imposed by this title with respect to such transaction shall not expire before the date which is 1 year after the earlier of—
>
> (A) the date on which the Secretary is furnished the information so required, or
>
> (B) the date that a material advisor meets the requirements of section 6112 with respect to a request by the Secretary under section 6112(b) relating to such transaction with respect to such taxpayer.

The term "listed transaction" means a transaction which is the same as, or substantially similar to, a transaction specifically indentified by the Secretary as a tax avoidance transaction for purposes of 26 U.S.C. § 6011 (2011). 26 U.S.C. § 6707A(c)(2) (2011).

IRS Notice 2000-44, 2000-36 I.R.B. 255, to which petitioner cites in its petition at footnote 1, was issued in response to the type of transaction at issue in this case—which, as mentioned above, has

since been labeled with the moniker "Son-of-BOSS". In that Notice, the IRS advised that "[t]ransactions that are the same as or substantially similar to the transactions described in this Notice 2000-44 are identified as "listed transactions" for the purposes of section 1.6011-4T(b)(2) of the Temporary Income Tax Regulations and section 301.6111-2T(b)(2) of the Temporary Procedure and Administration Regulations."

Thus, Congress has enacted a separate statute of limitations for all alleged tax shelters, including "Son-of-BOSS," entered into after the effective date of § 6501(c)(10). Congress added this provision to address a concern with respect to listed transactions without changing the six-year statute of limitations or overruling this Court's decision in *Colony*. Since *Colony* was decided, Congress has amended § 6501(e) nine times[3], yet it never changed the relevant language that was considered in *Colony*, and is controlling in this case. Congress certainly could have changed the law to overturn the rule in *Colony* if it saw fit. In fact, the same 2004 Act overturned the rule that resulted from *Sutherland Lumber-Southwest, Inc. v. Commissioner*, 114 T.C.

---

[3] *See* Hiring Incentives to Restore Employment Act of 2010, Pub. L. No. 111-147, § 513(a)(1); American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 413(c)(28); Revenue Act of 1978, Pub. L. No. 95-600, § 701(t)(3)(A); Black Lung Benefits Revenue Act of 1977, Pub. L. No. 95-227, § 4(d)(4); Tax Reform Act of 1976, Pub. L. No. 94-455, §§ 1307(d)(2)(F)(vi) and 1906(b)(13)(A); Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, § 1016(a)(14); Excise, Estate, and Gift Tax Adjustment Act of 1970, Pub. L. No. 91-614, § 102(d)(8); Tax Reform Act of 1969, Pub. L. No. 91-172, § 101(g)(3); Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, § 810(b).

197 (2000), *aff'd per curiam*, 255 F.3d 495 (8th Cir. 2001), with respect to the costs of entertainment, amusement or recreation-related goods, services, and facilities provided by private and publicly-held companies to "specified individuals". *See* 26 U.S.C. § 274(e)(2)(B), as enacted by Pub. L. No. 108-357, § 907 (2004). Congress chose to leave *Colony* intact and limit the new provision's application to certain tax shelters, including "Son-of-BOSS," going forward. If the transaction in this case had occurred after the effective date of this new statute, then § 6501(c)(10)—and not the six-year statute or the Regulation promulgated thereunder—would have dictated the period of limitation. Congress's decision to extend the statute of limitations for listed transactions prospectively supports the conclusion that Congress intended to leave the rule established in *Colony* intact for all other cases.

This is not the only case in which alleged "Son-of-BOSS" tax shelters are being litigated. Petitioner has alleged that other taxpayers, including those in *Beard v. Commissioner*, 633 F.3d 616, 622 (7th Cir. 2011), *petition for cert. filed*, 80 U.S.L.W. 3004 (U.S. June 23, 2011) (No. 10-1553), *Grapevine Imports, Ltd. v. United States*, 636 F.3d 1368 (Fed. Cir. 2011), *petition for cert. filed*, 80 U.S.L.W. 3090 (U.S. Aug. 5, 2011) (No. 11-163), *Burks v. United States*, 633 F.3d 347 (5th Cir. 2011), *petition for cert. filed*, 80 U.S.L.W. 3090 (U.S. Aug. 11, 2011) (No. 11-178), *Salman Ranch, Ltd. v. Commissioner*, --- F.3d ---, 2011 WL 2120044 (10th Cir. 2011) ("*Salman Ranch II*") and *Intermountain Insur. Servs. of Vail, LLC v. Commissioner*, --- F.3d ---, 2011 WL 2451011 (D.C.Cir. 2011), have

also engaged in the "Son-of-BOSS" tax shelter. These cases all involve essentially the same issue – the appropriate statute of limitations for a "Son-of-BOSS" transaction. In each case, petitioner contends that the six-year statute contained in § 6501(e)(1)(A) applies. The question is merely academic for taxpayers other than the parties involved in these cases because Congress has resolved the issue for future cases by enacting § 6501(c)(10).

This case is one that is important for the parties involved, but its resolution is not important for the public at large. *See Rice v. Sioux City Mem'l Park Cemetery*, 349 U.S. 70, 76, 77 n.1 (1955) (dismissing petition for certiorari because matter was no longer of public importance where underlying statute had been changed). Because Congress addressed petitioner's concerns raised by alleged "Son-of-BOSS" transactions in future cases when it enacted § 6501(c)(10), judicial economy dictates that this case does not rise to the level of public importance for this Court to grant petitioner's petition for writ of certiorari.

II. This Court's decision in *Colony* controls the statute of limitations period in this case.

The Fourth Circuit correctly decided that the outcome of this case is governed by *Colony*, in which this Court held that an overstatement of basis does not equate to an omission from gross income and, thus, cannot trigger the extended statute of limitations period set forth in § 6501(e)(1)(A). The

petition in this case is limited in substantive content, presumably due to the fact that petitioner would prefer the Court to hold this case in abeyance pending the Court's final disposition of petitioner's case of choice to address the issues raised here—*Beard*.[4] Nevertheless, respondents must address the issues, and the arguments raised by petitioner in both this petition and filings with the Court in similarly situated cases—such as *Beard*, *Grapevine* and *Burks*.[5]

---

[4] Although the petition for writ of certiorari in *Beard* was filed first in this line of cases, respondents disagree that it would be the best case for a petition to be granted if the Court is so inclined to review the issues present in these similarly situated cases. The Seventh Circuit's opinion in *Beard* is somewhat of an outlier because it only addresses the application of *Colony* to the facts, and fails to address the Regulation. Thus, *Beard* lacks sufficient analysis of all of the issues that have been analyzed and discussed in other cases.

[5] The Ninth Circuit followed this Court's decision in *Colony*, but did so prior to the promulgation of either the temporary or final Regulation. *See Bakersfield Energy Partners, LP v. Comm'r*, 568 F.3d 767 (9th Cir. 2009). The Fourth Circuit, here, and the Fifth Circuit have followed *Colony* in ruling against the IRS, even after the issuance of the temporary and final Regulation. *See Home Concrete*, *supra*; *Burks*, *supra*. The Federal, Seventh, Tenth, and District of Columbia Circuits—have declined to follow *Colony*. *See Grapevine*, *supra*; *Beard*, *supra*; *Salman Ranch II*, *supra*; *Intermountain*, *supra*. Interestingly, the Federal Circuit has an intra-circuit conflict in that it has also held in favor of the taxpayers with respect to the application of *Colony*—once before the Regulation became final, and once after. *See Salman Ranch, Ltd. v. United States*, 573 F.3d 1362 (Fed. Cir. 2009); *Grapevine*, *supra*.

In the event that the Court grants petitioner's request to hold this case in abeyance and, instead, issues a writ of certiorari in *Beard*, *Grapevine*, *Burks* or another case with similar questions presented, respondent respectfully request that the Court consider the law set forth herein.

With respect to the underlying issue of whether an overstatement of basis is an omission of gross income, petitioner makes strikingly similar arguments here to those it made in *Colony*—most notably, petitioner focuses on the statutory definition of "gross income" as opposed to the entire phrase "omits from gross income" and Congress' true intent exemplified in the legislative history when it enacted the statute. Petitioner has also consistently argued that this Court's decision in *Colony* is limited in application to situations involving sales of goods or services by taxpayers in a trade or business. These arguments continue to miss the target.

In order to understand the purpose of the statute in issue, it is imperative to have some knowledge of the pertinent cases that preceded *Colony* and led both to this Court's decision in that case and the additional subparagraphs to the statutory language in what is now § 6501(e)(1)(A).[6] Section 6501(e)(1)(A) as it existed in 1999 was enacted as part of the reform that resulted in the 1954 Internal Revenue Code, and was a recodification of 26 U.S.C. § 275(c) (1939). The earlier statute provided as follows:

> If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percentum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection

---

[6] Subparagraph (i) of § 6501(e)(1)(A) is generally referred to here as the "gross receipts provision," while subparagraph (ii) is referred to as the "adequate disclosure provision".

> of such tax may be begun without assessment, at any time within 5 years after the return was filed.

Id.

Prior to *Colony*, several Circuit courts addressed the issue of whether an overstatement of cost or basis, resulting in an understatement of "the final figure in [the] gross income computation" constituted an "omi[ssion] from gross income" as contemplated by Congress when it added 26 U.S.C. § 275(c) (1939). *See, e.g.*, *Uptegrove Lumber Co. v. Comm'r*, 204 F.2d 570 (3d Cir. 1953). One of the first cases to address this issue was decided by the Court of Appeals for the Sixth Circuit. *Reis v. Comm'r*, 142 F.2d 900 (6th Cir. 1944). In *Reis*, the Sixth Circuit found that there was an omission of gross income where the taxpayer in question overstated his basis in certain pieces of property that he sold. Citing *Ewald v. Comm'r*, 141 F.2d 750 (6th Cir. 1944), a case in which there was no overstatement of basis involved, the court summarily determined that the taxpayer in *Reis* omitted gross income. *Reis*, 142 F.2d at 903.

Years later, in *Uptegrove Lumber*, the Court of Appeals for the Third Circuit faced a similar issue to that faced in *Reis*, where the taxpayer was a manufacturing corporation and inappropriately included a reserve for retroactive wage increases in its cost of goods sold—thus, arriving at an incorrect gross profit from sales. *Uptegrove Lumber* was the first case where the question of whether "the language 'omits from gross income any amount

properly includible therein' should be read broadly as if it read 'understates the final figure in [a taxpayer's] gross income computation'" was thoroughly addressed by a court in an opinion. *Uptegrove Lumber*, 204 F.2d at 571.

In its review of what constitutes an omission from gross income, the Third Circuit noted Treasury Regulation 111, 29.22(a)-5, now found in substantially similar form in Treasury Regulation § 1.61-3(a), which provided "[i]n the case of a manufacturing, merchandising, or mining business, 'gross income' means the total sales, less the cost of goods sold, plus any income from investments and from incidental or outside operations or sources***." *Id.* The court also cited to the "numerous provisions of 26 U.S.C. § 22 [(1939)]," which preceded the current provision defining gross income in 26 U.S.C. § 61 (1999), as "controlling the computation of gross income, generally."[7] *Id.* Despite specifically

---

[7] Paragraph (a) of 26 U.S.C. § 22 (1939) provided as follows:

> (a) GENERAL DEFINITION. – "Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross

recognizing the regulatory definition of gross income for purposes of certain trades or businesses and the statutory definition of gross income generally, the Third Circuit reviewed the legislative history[8] and concluded that "the history of Section 275(c) persuasively indicates that Congress was addressing itself particularly to the situation where a taxpayer shall fail to include some receipt or accrual in his computation of gross income and not in a more general way to errors of whatever kind in that computation." *Id.* at 572.

In the three years following *Uptegrove Lumber*, the Ninth, Fifth and Eighth Circuits each issued opinions barring an extension of the statute of limitations in situations where the taxpayers included their gross receipts, but erred in their computation of taxable income. *See Slaff v. Comm'r*, 220 F.2d 65 (9th Cir. 1955); *Davis v. Hightower*, 230

> income; and all Acts fixing the compensation of such Presidents and judges are hereby amended accordingly.

Both 26 U.S.C. § 22 (1939) and 26 U.S.C. § 61 (1999) notably include "gains" in the definition.

[8] In *Uptegrove Lumber*, the court addressed the IRS's reference to Congress's occasional use of the phrase "understates gross income" in the relevant Committee reports, and reasoned: "wherever this language appears it is used in the generality of an introductory statement and is immediately restricted by specific explanation that the Committee is talking about 'failure to disclose' income or ' leaving out items.'" *Id.* at 572. The court then points to a particularly striking instance in the House Subcommittee Report where the reference to "understatement" is "'that the limitation period on assessments should not apply *to certain cases* where the taxpayer has understated the gross income'". *Id.*

F.2d 549 (5th Cir. 1956); *Goodenow v. Comm'r*, 238 F.2d 20 (8th Cir. 1956). The foregoing cases set the stage for this Court's opinion in *Colony*. In *Colony*, the IRS alleged that a taxpayer "understated the gross profits on the sales of certain lots of land for residential purposes as a result of having overstated the 'basis' of such lots by erroneously including in their cost certain unallowable items of development expense." *Id.* at 30. After the Tax Court found that the extended statute should apply, the Sixth Circuit again faced the question it had addressed in *Reis* 13 years earlier. Despite the clear conflict in interpretation of the statute with the Third, Fifth, Eighth and Ninth Circuits, the Sixth Circuit held firm, noting that the "reasoning of these cases is not without considerable persuasive force, and if the question were here for the first time, we might be disposed to follow them." *See Colony, Inc. v. Commissioner*, 244 F.2d 75 (6th Cir. 1957). Ultimately, however, the court deferred to the authority of its precedential decision in *Reis* and affirmed the Tax Court's decision.

After granting certiorari, this Court began its review with the "critical statutory language," focusing on the definition of the word "omits" and approving the dictionary definition "to leave out or unmentioned; not to insert, include, or name." *Colony*, 357 U.S. at 32. Although the Court was "inclined to think that the statute on its face lends itself more plausibly to the taxpayer's interpretation," it turned to the legislative history to determine Congress's intent. The legislative history confirmed that the statute should be extended only in specific situations when taxpayers "leave out

items" or a taxpayer "overlooks an item," "failed to report a dividend," or "might report as income for one year an item of income which properly belonged in another year." *Id.* at 33-35. The Court cited these instances as "persuasive indications that Congress merely had in mind failures to report *particular income receipts and accruals*, and did not intend the five-year [now six-year] limitation to apply whenever gross income was overstated." *Id.* at 35 (emphasis added). In the end, this Court agreed with the taxpayer's position that "the statute is limited to situations in which specific receipts or accruals of income items are left out of the computation of gross income." *Id.* at 33 (emphasis added).

This Court found that Congress's purpose for enacting the extended assessment period was "no broader...than to give the Commissioner an additional two years [now three years] to investigate tax returns in cases where because of the taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors." *Id.* The extended assessment period applies only in instances where "the return on its face provides no clue to the existence of the omitted item." *Id.* The Court concluded, "when as here, the understatement of a tax arises from an error in reporting an item disclosed on the face of the return the Commissioner is at no such disadvantage." *Id.* Citing *Uptegrove Lumber*, the Court later stated that to accept the Commissioner's interpretation of the statute "not only would be to read s 275(c) more broadly than is justified by the evident reason for its enactment, but also to create a

patent incongruity in the tax law." [9] *Colony*, 357 U.S. at 36-37.

Although the version of the Code that this Court interpreted in *Colony* had been revised and renumbered between the tax years in issue and the year of the decision, the Court noted that its conclusion was "in harmony with the *unambiguous* language of § 6501(e)(1)(A)," the same statute at issue in the present case. *Id.* at 37 (emphasis added).

A. Colony is not limited to cases involving the sale of goods or services in a trade or business.

Petitioner argues that *Colony* is distinguishable from this case because its holding is *limited* to cases involving a trade or business selling

---

[9] The citation to *Uptegrove Lumber* is to page 573, which provides in relevant part:

> For there are many places throughout an income tax return where a taxpayer may make arithmetical errors or claim improper deductions with the result that his tax liability is understated. If such errors are made in good faith at any place other than the gross income section, it is clear that the government must challenge them, if at all, within the normal three year limitation period. No reason appears or has been suggested why Congress would wish to allow a longer time to discover errors of the same type in the gross income section of the return. Yet this would be the strange result of the construction which the Commissioner would give to Section 275(c).

goods or services.[10] Petitioner's argument is untenable for several reasons. First, the assertion that land can constitute a "good"—which is required in order to fall under the authority of the gross receipts provision—is simply incorrect. More importantly, petitioner's argument conflicts directly with its historical position on the classification of land and buildings as other than merchandise or "goods."[11] Specifically in the context of overstated basis cases, the IRS argued that a ranch could not constitute a "good" in its brief in *Salman Ranch I*, which was decided in favor of the taxpayers:

> Ordinarily, the term "goods" does not encompass a ranch. The term "goods" typically means "tangible movable

---

[10] In *Colony*, the IRS alleged that a taxpayer "understated the gross profits on the sales of certain lots of land for residential purposes as a result of having overstated the 'basis' of such lots by erroneously including in their cost certain unallowable items of development expense." *Id.* at 30. While there is no definition of "goods" in the Internal Revenue Code, it is doubtful that real property would be included. "Goods" in other areas of the law have traditionally only included personal property. *See, e.g.*, U.C.C., Art. 9, § 9-102(a)(44) ("'Goods' means all things that are moveable when a security interest attaches.").

[11] *See* Patrick J. Smith, *"Omissions From Gross Income and 'Numerators and Denominators'"* SPECIAL REPORT TAX NOTES, 157, 161-163 (July 11, 2011) (citing *W.C. & A.N. Miller Dev. Co. v. Commissioner*, 81 T.C. 619, 630 (1983) ("In our view, real property should not be considered as 'merchandise' within the contemplation of the regulation....In its commonly accepted usage, the term 'merchandise' is defined to encompass wares and goods, not realty"); *Homes by Ayres v. Commissioner*, 795 F.2d 832, 835 (9th Cir. 1986) ("The Commissioner has consistently maintained that real property cannot be inventoried for tax purposes")).

> personal property having intrinsic value usually excluding money and other choses in action." Webster's Third New Int'l Dictionary 978 (1969). See also Black's Law Dictionary at 701 (7th ed. 1999) (defining "goods" as "[t]angible or movable personal property other than money; especially articles of trade or items of merchandise," as in "goods and services").
>
> ...
>
> [The taxpayers'] reliance (Br. 34) on the definition of "goods or services" in the unrelated context of charitable contributions in Treas. Reg. § 1.170A-13(f)(5) is misplaced....In that context, § 1.170A-13(f)(5) defines "goods or services" as "cash, property, services, benefits, and privileges." Significantly, real estate is not included; thus, even if the regulation somehow applied here, it would not make the ranch a "good[ ] or service [ ]."

Brief for the Appellee at 45-49, *Salman Ranch I*, No. 2008-5053 (citations omitted).[12] The same definition of "goods" would have applied to the land sold in *Colony*. Thus, petitioner's argument that *Colony*'s holding is limited to situations involving the sale of goods or services in a trade or business defies reason when *Colony* itself would not have fallen within that category.

---

[12] *See also* Smith, *supra* at n.11.

Furthermore, the Court in *Colony* stated that its "construction of s 275(c) accords with the interpretations in the more recent decisions of four different Courts of Appeals. *See* note 2, *supra*." *Colony*, 357 U.S. at 37. Note 2 in *Colony* cites to *Uptegrove Lumber*, *Slaff*, *Davis* and *Goodenow*, decided by the Third, Ninth, Fifth and Eighth Circuits, respectively. *Colony*, 357 U.S. at 32, n.2. Of particular note is *Slaff*, which had nothing to do with the sale of goods or services in a trade or business. To the contrary, the taxpayer in *Slaff* reported an amount he received while working for the American Red Cross while serving in Europe during World War II, but claimed that it was exempt from taxation—resulting in an understatement of taxable income. If *Colony* was intended to be limited to cases involving the sales of goods or services in a trade or business, then it certainly would not have accorded its decision with the Ninth Circuit's decision in *Slaff*.

Finally, the Court's opinion includes no language limiting its opinion to particular situations involving sales of goods or services in a trade or business to the exclusion of other situations. The more reasonable view is that *Colony* was intended to bar the extension of the statute of limitations where the taxpayer overstated its basis, resulting in an understatement of taxable income, but not an omission of items of gross income. As Judge Wynn poignantly stated in the Fourth Circuit opinion in this case "the Supreme Court in *Colony* straightforwardly construed the phrase 'omits from gross income,' unhinged from any dependency on the taxpayer's identity as a trade or business selling

goods or services." *Home Concrete*, 634 F.3d at 255. Accordingly, *Colony* properly controls the outcome of this case.

B. The gross receipts and adequate disclosure provisions are not superfluous.

The petition focuses on the statutory definition of "gross income", and particularly on the inclusion of "gain" in such definition, in § 61, and the underlying regulations. Petitioner also confuses "gross income" with "taxable income", just like it did more than 50 years ago, when it states: "[b]ecause the *taxable income* from a property sale is generally determined by subtracting the taxpayer's basis from the property's sale price, an overstatement of basis will typically decrease the amount of the taxpayer's gain (and thus the amount of federal income-tax liability) that is attributable to the sale." Pet. Cert. 2-3. As this Court and the circuit courts that faced this issue prior to *Colony* made very clear, the statutory definition of "gross income" and § 275(c) had not yet been considered together. This Court focused on the entire phrase "omits from gross income," not just the statutory definition of "gross income"—which is substantially the same as it was at the time *Colony* was decided—when it concluded that an omission only occurs when items of income are left out of the return. Petitioner's rehashed argument was unpersuasive when this Court decided *Colony* and should not prevail here.

Petitioner has argued that, if *Colony*'s decision applies to all cases, and the general rule is that an overstatement of basis cannot give rise to an

omission of gross income, then the amendments added to the statute in 1954 would be superfluous. *See Beard* Pet. Cert. 12 (citing *Intermountain*). The foregoing discussion of the cases leading up to *Colony* demonstrates that such is not the case; rather, those amendments were added to clarify that "omits" means "failure to disclose" income or "leaving out items" of income no matter who the taxpayer is.

The reasoning for the inclusion of the gross receipts provision is best demonstrated in the Third Circuit's opinion in *Uptegrove Lumber*, which was a case involving a manufacturing corporation decided in 1953—the year prior to the amendment to the statute. As mentioned above, the Third Circuit decided that despite the definition of gross income in the regulations for "a manufacturing, merchandising, or mining business," which included the total sales, less the cost of goods sold, the legislative history was clear that the intent of Congress was to extend the statute only in situations where an item of income was left out—not when there was an error in the computation. Thus, the Third Circuit decided the case in favor of the taxpayer, who happened to be a trade or business. The same error in computation simply had not come along in the case of a non-trade or business—i.e., there *was no need to clarify* the statute for cases other than trades or businesses.

It is important to note that there is no discussion in the legislative history to the statutory amendments, and no evident policy reason for treating the sales of goods or services in a trade or business differently (and, arguably, more favorably) than income derived by an individual or trade or

business that makes an error in computation of their taxable income. The better, more sensible, explanation for the gross receipts provision of § 6501(e)(1)(A)(i) is simply that it was added to codify the result in *Uptegrove Lumber* in the context of a trade or business—because a need for a clarification in that particular circumstance had been brought to the attention of Congress immediately prior to enacting the gross receipts provision.

In 1956, the Fifth Circuit in *Davis*, which preceded *Colony* but, as mentioned above, was cited as being in accord with this Court's decision,[13] explained the purpose of adding the adequate disclosure provision now found in § 6501(e)(1)(A)(ii):

> It cannot be thought that if a taxpayer accurately fills in every blank space provided for his use in the income tax form, giving every "gross" or maximum figure called for, and arrives at an incorrect computation of the tax only by reason of a difference between him and the Commissioner as to the legal construction to be applied to a disclosed transaction, the use of a smaller figure than that ultimately found to be correct in one stage of the computation amounts to an omission from 'gross income' of the difference between the correct and incorrect item.
>
> ...

---

[13] *See Colony*, 357 U.S. at 37.

> To [the] legislative history is now added the amendment contained in the 1954 Internal Revenue Code, under the terms of which it is now clear that the inclusion of the statement made by appellee in his return here would be sufficient to prevent application of the five year statute. In view of the confusion as to the meaning of the statute prior to the adoption of the 1954 Code, we think it plain that the new language was enacted to *clarify the existing law*.

Davis, 230 F.2d at 553-554 (emphasis added). In other words, "gross" means "gross", not "net" as petitioner argues.[14] Accepting petitioner's argument would create precisely the "patent incongruity" in the tax law that this Court specifically rejected in *Colony*.

The Fifth Circuit's interpretation of the proper application of the statute was confirmed in this Court's opinion in *Colony*. The purpose of the amendments was to clarify that, notwithstanding statutory or regulatory definitions of gross income or prior cases to the contrary, if all "gross" items are disclosed in the return of any taxpayer, then the statute should not be extended. Accordingly, neither

---

[14] As the Fifth Circuit stated in *Davis* with respect to the general understanding of what constituted "gross income," "such figure as used *in an ordinary or accounting sense* is not an ingredient in the total that is finally subject to the application of the tax rates." *Davis*, 230 F.2d at 553 (emphasis added).

amendment to the current statute is made superfluous by applying this Court's decision in *Colony* to cases other than those involving the sale of goods or services in a trade or business.

III. The Regulation is inapplicable to this case.

On September 28, 2009, soon after the Ninth and Federal Circuits followed this Court's decision in *Colony* and held in favor of the taxpayers in *Bakersfield* and *Salman Ranch I*, *supra*, the Treasury rushed to issue a new temporary Treasury Regulation in an attempt to overturn the rule set forth in *Colony* that an overstatement of basis cannot create an omission from gross income. Temp. Treas. Reg. § 301.6501(e)-1T. The temporary regulation was made immediately effective by the Treasury without notice or an opportunity for comment by the public. *Id.* The Treasury published the regulation in final form without any material changes on December 17, 2010. Treas. Reg. § 301.6501(e)-1. In relevant part, the Regulation provides that "an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A)." *Id.*

The Regulation represents a sweeping change from the clear intent of Congress in the legislative history as discussed in this Court's opinion in *Colony*. Prompted by losses in *Bakersfield* and *Salman Ranch I*, each of which also allegedly involved a "Son-of-BOSS" tax shelter, the Treasury claimed in the preamble to the temporary Regulation

that it would merely "clarify" the meaning of § 6501(e)(1)(A).[15] To the contrary, the Regulation is a blatant attempt to overturn the rule set forth in this Court's opinion in *Colony*, and would have a much broader application to all cases where an error might result in an understatement of taxable income. *See, e.g.*, *Wilmington Partners L.P., et al. v. Comm'r*, Tax Court Docket No. 15098-06, appeal filed No. 10-4183 (2d Cir. filed Oct. 13, 2010) (involving the question of whether an alleged overstatement of basis creates an omission of gross income such that the statute of limitations should be extended where no tax shelter transaction occurred).

A. The Regulation does not apply by its own terms, is an abuse of executive power and violates due process.

The Regulation provides that it "applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009." Treas. Reg. § 301.6501(e)-1(e)(1). By its terms, it is inapplicable to this case. Despite the Treasury's claim that a six-year statute remains open for all cases pending before a court of competent jurisdiction—the question whether the period for assessing tax was open more than three years after the relevant returns were filed in this case is precisely what is in question and must be decided by this Court. Even if the Regulation were

---

[15] *See* T.D. 9466 (citing *Bakersfield* and *Salman Ranch I* as wrongly interpreting *Colony*); *see also* T.D. 9511 (preamble to final Regulation).

deemed valid, it is moot if the six-year period applies here without reference to it.

Should the Court determine that the Regulation is viable despite Congress's enactment of § 6501(c)(10) and the circular logic resulting from its effective date provision, respondents contend that it should be rendered invalid based on the hardship and prejudice its retroactive application would cause. The IRS's authority to issue retroactive regulations is subject to review for abuse of discretion. *Chock Full O'Nuts Corp. v. U.S.*, 453 F.2d 300, 302 (2d Cir. 1971). "'The Internal Revenue Service does not have *carte blanche*. Its choice must be a rational one, supported by relevant considerations.'" *Id.* (citing *Int'l Bus. Machs. Corp. v. U.S.*, 343 F.2d 914, 920 (Ct. Cl. 1965)).

> [C]ourts have declined to give retroactive effect to regulations or rulings of the Commissioner when retroactivity would work a change in settled law relied on by the taxpayer and implicitly approved by Congress, *Helvering v. R.J. Reynolds Tobacco Co.*, 306 U.S. 110...(1939), when it would lead to inequality of treatment between taxpayers, [*Int'l Bus. Machs. Corp.*, *supra*], when litigation involving the area clarified by the regulation had already begun, *Commissioner of Internal Revenue v. Goodwyn Crockery Co.*, 315 F.2d 110, 113 (6th Cir. 1963), or when, in general, the result of retroactivity in a particular case would be unduly harsh, *Lesavoy Foundation v.*

> *Commissioner*, 238 F.2d 589, 594 (3d Cir. 1956); cf. *Woodward v. United States*, 322 F.Supp. 332, 335 (W.D.Va. 1971).

Id. at 302, n. 6.

Respondents filed suit in December 2006, more than six years after the relevant returns were filed with the IRS and nearly three years before the Regulation was promulgated in temporary form. The Regulation was issued in an attempt to guarantee a win for the IRS in this case, in which it is a party, and to revive and overturn various losses suffered in similarly situated cases in other jurisdictions. Respondents clearly relied on *Colony* when they filed their complaint in this case.

Petitioner argues that it is not changing the law retroactively. Rather, it maintains it is merely "clarifying" the law with its Regulation. As discussed above, and as recognized by the Fourth Circuit below, the Regulation changes the law that was settled by this Court over 50 years ago, while Congress has remedied any abuse that might result from an undisclosed listed transaction in the future. Respondents have expended substantial time, energy, and financial resources (in litigation costs, including legal fees and, potentially, in continuously accruing interest) with the expectation that they were fighting on a level playing field, and would ultimately prevail on the statute of limitations issue based on longstanding Supreme Court precedent. The Regulation purports to dictate the outcome

without any regard for due process[16] or fair treatment of the taxpayers. Accordingly, the regulation should be struck down.

B. The Regulation does not deserve *Chevron* deference.

Even if the Regulation is analyzed under the test set out in *Chevron U.S.A Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), it is not entitled to deference. *Chevron* provides a two-step analytical framework. "First, always, is the question whether Congress had directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." *Id.* at 842-43. This Court clarified step one in the analysis in a footnote:

> The judiciary is the final authority on issues of statutory construction and must reject administrative constructions which are contrary to clear congressional intent.... If a court, employing *traditional tools of statutory*

---

[16] In *United States v. Carlton*, 512 U.S. 26, 32-33 (1994), this Court held that, under the Due Process Clause of the Fifth Amendment in the Constitution, Congress may adopt retroactive tax rules only when they are rationally related to a valid government purpose and only when the period of retroactivity is "modest." The Regulation was issued more than 9 years after the returns were filed here and would be trumped by 26 U.S.C. § 6501(c)(10) with respect to Son-of-BOSS transactions in the future. Given the extended period of retroactivity and lack of a valid government purpose, the Regulation violates due process.

> *construction*, ascertains that Congress had an intention on the precise question at issue, that intention is the law and must be given effect.

Id. at 843, n.9 (emphasis added). If the Court cannot determine that "Congress had an intention on the precise question at issue," the second step in the analysis requires the Court to answer whether the agency's interpretation is permissible or reasonable. *Id.* at 843-844.

This Court in *Chevron* utilized legislative history as part of its step one analysis, and has continued to do so in more recent opinions. *Id.* at 862; *see also Zuni Pub. Sch. Dist. No. 89 v. Dept. of Educ.*, 550 U.S. 81, 90-91 (2007); *Gen. Dynamics Land Sys., Inc. v. Cline*, 540 U.S. 581, 587-90, 600 (2004). The IRS has persistently cited the Supreme Court's statement that "it cannot be said that the language is unambiguous" when referring to the term "omits from gross income" in arguing that such language remains ambiguous. However, reliance on this statement ignores this Court's subsequent review of the statute's legislative history—and the importance placed on Congress's intent found in the legislative history in the cases that preceded *Colony*. In *Colony*, this Court confirmed the plain meaning of the statutory language "omits from gross income" by referring to legislative history and repeatedly emphasizing Congress's intent that the statute should be extended only in specific situations when taxpayers "leave out items" or a taxpayer "overlooks an item," "failed to report a dividend," or "might report as income for one year an item of income which properly belonged in another year." *Colony*,

357 U.S. at 33-35. The Court cited these instances as "persuasive indications that Congress merely had in mind *failures to report particular income receipts and accruals*, and did not intend the five-year [now six-year] limitation to apply whenever gross income was overstated." *Id.* at 35 (emphasis added).

After reviewing the legislative history, this Court clarified that the only reasonable interpretation of the term "omits from gross income" involves leaving out an actual item of income, and not an overstatement of tax basis. Any uncertainity was resolved by the Court over 50 years ago. In addition, Congress has consistently refused to change the relevant language in § 6501(e), and has affirmatively acted by enacting § 6501(c)(10). The Regulation conflicts directly with this Court's construction of the statutory language and the unambiguous intent of Congress. Accordingly, the Regulation fails under *Chevron* step one.[17]

C. *Brand X* does not control.

In *Brand X*, this Court found that the circuit court's prior decision held only that the *best reading* of the statute in question was that a cable modem service was a "telecommunications service," not that it was the *only permissible reading* of the statute. *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 982, 984 (2005). The Court added that "[a] court's prior judicial construction of a

---

[17] If it is determined that the Regulation passes muster under *Chevron* step one, as we argue here, it is nevertheless unreasonable in light of Congress' enactment of § 6501(c)(10). If a "gap" remained in the statute, Congress has filled it. *See Chevron*, 467 U.S. at 842.

statute trumps an agency construction otherwise entitled to *Chevron* deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion." *Id.* at 982.

In a concurring opinion, Justice Stevens suggested that the majority's explanation of "why a court of appeals' interpretation of an ambiguous provision in a regulatory statute does not foreclose a contrary reading by the agency...would not necessarily be applicable to a decision by [the Supreme] Court that would presumably remove any pre-existing ambiguity. *Id.* at 1003 (J. Stevens, concurring).

In *Colony*, this Court stated:

> "[w]e find in that [legislative] history persuasive evidence that Congress was addressing itself to the specific situation where a taxpayer actually omitted some income receipt or accrual in his computation of gross income, and not more generally to errors in that computation arising from other causes...
>
> *We have been unable to find any solid support of the Government's theory in the legislative history.* Instead..., this history shows to our satisfaction that the Congress intended an exception to the usual three-year statute of limitations *only* in the restricted type of situation already described.

Colony, 357 U.S. at 33, 36 (emphasis added). This statement demonstrates that this Court's interpretation was the *only permissible reading* and not only the *best* reading. While the Court did not use the explicit language described in *Brand X*, it is unreasonable to expect, or require, that the *Colony* decision would give the terms 'ambiguous' and 'unambiguous' the special meaning assigned to them by the *Chevron* decision 26 years later.[18] More pointedly, this Court ultimately concluded in *Colony* that the language of § 6501(e)(1)(A) was unambiguous, and its decision therein was "in harmony" with the current statute. *Colony*, 357 U.S. at 37.

The Regulation blatantly oversteps the authority of an agency by attempting to retroactively legislate a substantive change in the law in order to force a victory in this case and other similarly situated cases—while Congress has remedied any concern with respect to cases involving a "Son-of-BOSS" statute of limitations issue going forward. There is no question that this Court's jurisprudence has developed over the years to give substantial deference to agencies in interpreting ambiguities in the law. *See Chevron*; *see also Mayo Found. For Med. Educ. & Research v. United States*, 562 U.S. ___ (2011); *Brand X*. However, there must be a line drawn where an agency's powers end, and those more appropriately controlled by Congress or this Court take over. As Judge Wilkinson stated succinctly in his concurrence below:

---

[18] *See* Patrick J. Smith, *Brand X and Omissions from Gross Income*, TAX ANALYSTS, 665, 670 (Feb. 1, 2010).

> Yet it remains the case that agencies are not a law unto themselves. No less than any other organ of government, they operate in a system in which the last words in law belong to Congress and the Supreme Court. What the IRS seeks to do in extending the statutory limitations period goes against what I believe are the plain instructions of Congress, which have not been changed, and the plain words of the Court, which have not been retracted.

Home Concrete, 634 F.3d at 259. Accordingly, the Regulation cannot overturn this Court's decision in *Colony*.

CONCLUSION

Because *Colony* controls, and the conflict in issue would likely not exist if the same facts existed today due to the enactment of § 6501(c)(10), judicial economy dictates that granting the petition for writ of certiorari in this case would be a waste of this Court's time and resources. Accordingly, respondents respectfully request that the Court deny the petition for writ of certiorari in this case.

Respectfully submitted.

Richard T. Rice
Counsel of Record
Charles M. Wiley
Michael R. Cashin
Robert T. Numbers, II
WOMBLE CARLYLE SANDRIDGE & RICE, PLLC
One West 4th Street
Winston-Salem, North Carolina 27101
(336) 721-3609
rrice@wcsr.com

Counsel for Respondents

REPLY BRIEF

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

DONALD B. VERRILLI, JR.
Solicitor General
Counsel of Record
Department of Justice
Washington, D.C. 20530-0001
SupremeCtBriefs@usdoj.gov
(202) 514-2217

TABLE OF CONTENTS

Page

A. The questions presented warrant this Court's review 2
B. *Beard* is the appropriate vehicle for this Court's review 5
Conclusion 8

TABLE OF AUTHORITIES

Cases:

AD Global Fund, LLC v. *United States*, 481 F.3d 1351 (Fed. Cir. 2007) 3
Bakersfield Energy Partners, LP v. *CIR*, 568 F.3d 767 (9th Cir. 2009) 4
Beard v. *CIR*, 633 F.3d 616 (7th Cir. 2011), petition for cert. pending, No. 10-1553 (filed June 23, 2011) 1, 6
Chevron U.S.A. Inc. v. *NRDC*, 467 U.S. 837 (1984) 6

Statutes:

American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 814(b), 118 Stat. 1581 5
26 U.S.C. 6229(a) 3
26 U.S.C. 6501(a) 3, 4, 5
26 U.S.C. 6501(c)(10) 3, 4, 5
26 U.S.C. 6501(c)(10) (2004) 3
26 U.S.C. 6501(e)(1)(A) 2, 3, 4, 5, 6
26 U.S.C. 6707A(c)(2) (2011) 4

Miscellaneous:

Notice 2000-44, 2000-36 I.R.B. 255 4

In the Supreme Court of the United States

No. 11-139

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

The questions presented in this case are also presented in an earlier-filed petition for a writ of certiorari that is currently pending before the Court. See *Beard* v. *CIR*, 633 F.3d 616 (7th Cir. 2011), petition for cert. pending, No. 10-1553 (filed June 23, 2011). The government agrees with the petitioners in *Beard* that review should be granted in that case, and the government has therefore urged (Pet. 7-8) that the petition in this case be held pending the disposition of *Beard*.

Respondents argue that the questions presented do not warrant this Court's review. Amicus Bausch & Lomb Incorporated does not make that argument, but contends instead that, if this Court grants plenary review at all, it should do so in this case rather than in *Beard*. Both of those contentions lack merit. The questions presented are important and are the subject of a deep conflict among the courts of appeals. Because

Beard fully presents those questions and is the first-filed petition, the Court should grant review in that case.

A. The Questions Presented Warrant This Court's Review

1. This case concerns whether an understatement of gross income attributable to an overstatement of basis in sold property is an "omi[ssion] from gross income" that can trigger the six-year assessment period in 26 U.S.C. 6501(e)(1)(A). As the government explained in its brief in *Beard*, that issue warrants this Court's review. See Gov't Br. 19-20, *Beard*, *supra*. The Seventh, Tenth, Federal, and District of Columbia Circuits have held—based on either the text of Section 6501(e)(1)(A) or on a recently-promulgated Treasury regulation—that an understatement of gross income resulting from an overstatement of basis in a sold asset can trigger the six-year assessment period. *Ibid.* The court below and the Fifth Circuit have held to the contrary. *Id.* at 20.

The number of recent court of appeals decisions addressing this question reflects the importance of the issue to the Internal Revenue Service (IRS) and taxpayers. Because the nature of the transactions at issue makes them very difficult for the IRS to detect, see Gov't Br. 5, *Beard*, the IRS's ability to assess additional income tax often depends on the availability of the six-year assessment period. Because those additional taxes are on unreported capital gains of hundreds of millions of dollars, resolution of the issue would have a substantial impact on the United States Treasury. Moreover, there is a significant governmental and public interest in the uniform administration of federal tax law. Accordingly, this Court should grant review to resolve the conflict among the circuits.

2. Respondents do not dispute that the issue is important to the public fisc or that it is the subject of a circuit conflict. Respondents contend (Br. in Opp. 4-8), however, that this Court's review is no longer necessary because the issue has effectively been resolved by the enactment of 26 U.S.C. 6501(c)(10) (2004). That contention is incorrect for several reasons.

a. As an initial matter, respondents' argument reflects a misunderstanding of how 26 U.S.C. 6501(c)(10) operates. Section 6501(c)(10) does not create "a separate statute of limitations for all alleged tax shelters." Br. in Opp. 6. Indeed, Section 6501(c)(10) does not create a statute of limitations at all. Rather, Section 6501(c)(10) authorizes the extension of other tax assessment periods when certain criteria are satisfied. Specifically, Section 6501(c)(10) provides that "[i]f a taxpayer fails to include" on his return certain information about a "listed transaction," then "the time for assessment of any tax * * * with respect to such transaction *shall not expire*" until one year after the earlier of two events (both of which involve disclosure to the IRS of the relevant information). 26 U.S.C. 6501(c)(10)(A)-(B) (emphasis added). Section 6501(c)(10) thus may extend other tax assessment periods in certain cases when a taxpayer's return does not provide the specified information and the taxpayer then fails to disclose that information to the IRS after the return is filed.

Section 6501(c)(10) does not, however, replace other tax assessment periods, including the three- and six-year assessment periods in Sections 6501(a) and (e)(1)(A). See *AD Global Fund, LLC* v. *United States*, 481 F.3d 1351, 1354 (Fed. Cir. 2007) (construing the phrase "shall not expire before" in 26 U.S.C. 6229(a) to establish "a minimum period during which the period for

tax assessments for partnership items may not end"). For instance, Section 6501(c)(10) would not affect the running of either assessment period in Section 6501 if a taxpayer failed to provide information about a listed transaction on his return but disclosed the information to the IRS immediately thereafter. If such a taxpayer had understated his gross income by overstating his basis in property, it would remain necessary to decide which assessment period applies: the three-year period in Section 6501(a) or the six-year period in Section 6501(e)(1)(A). The issue in this case thus continues to have practical significance even with respect to tax returns filed after the enactment of Section 6501(c)(10).

b. Respondents are also incorrect in assuming (Br. in Opp. 4) that the questions presented here arise only in cases involving listed transactions. It is true that respondents participated in a Son-of-BOSS tax shelter, see Pet. 3; that a "listed transaction" includes any transaction identified by the IRS as one designed to avoid the payment of federal taxes, see 26 U.S.C. 6707A(c)(2) (2011); and that the IRS has identified Son-of-BOSS shelters as tax-avoidance transactions, see Pet. 4 n.1 (citing Notice 2000-44, 2000-36 I.R.B. 255). But the issue here—whether the six-year assessment period applies when a taxpayer understates his gross income by overstating his basis in a sold asset—can also arise in cases that do not involve Son-of-BOSS shelters or any other type of "listed transaction." See, *e.g.*, *Wilmington Partners L.P.* v. *CIR*, No. 10-4183 (2d Cir.) (argued Aug. 26, 2011); *Bakersfield Energy Partners, LP* v. *CIR*, 568 F.3d 767 (9th Cir. 2009); see also Amicus Br. 2 (acknowledging that "[t]he underlying transaction in *Wilmington Partners* does not involve a marketed tax shelter or so-called 'listed transaction'").

c. Finally, although this case does involve a listed transaction, Section 6501(c)(10) has no bearing on the ultimate resolution of the disputed timeliness issue. Section 6501(c)(10) applies to "taxable years with respect to which the period for assessing a deficiency did not expire before the date of the enactment of this Act," *i.e.*, October 22, 2004. American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 814(b), 118 Stat. 1581. Respondents filed their returns in April 2000. See Pet. 6 n.3. If respondents are correct that the "period for assessing a deficiency" was three years under Section 6501(a), then Section 6501(c)(10) does not apply to this case because the returns were filed more than three years before October 22, 2004. See Br. in Opp. 4 n.2. If (as the government contends) the "period for assessing a deficiency" was six years under Section 6501(e)(1)(A), then Section 6501(c)(10) could apply, but the government has no need to rely on it, since the challenged assessment would be timely in any event. See Pet. 6 n.3. In either event, Section 6501(c)(10) is ultimately irrelevant to the timeliness of the disputed IRS assessment.

Thus, notwithstanding Section 6501(c)(10)'s enactment, the proper disposition of this case ultimately turns on whether the IRS had three or six years to assess additional income taxes. And, as the recent proliferation of court of appeals decisions on that issue attests, the number of cases in which that will be so is sufficiently large to warrant this Court's review.

B. *Beard* Is The Appropriate Vehicle For This Court's Review

Amicus does not argue that this Court's review is unwarranted. Rather, it contends that, if this Court grants any of the pending certiorari petitions that present this

question, it should do so in this case rather than in *Beard*. The petitioners in *Grapevine Imports, Ltd.* v. *United States*, petition for cert. pending, No. 11-163 (filed Aug. 5, 2011) (*Grapevine*), have likewise claimed that their case is a better vehicle than *Beard*. Both amicus here and petitioners in *Grapevine* emphasize that the courts of appeals in the respective cases addressed the question whether a recently issued Treasury regulation was entitled to deference. See Amicus Br. 18-20; Pet. 32, *Grapevine*. The Seventh Circuit in *Beard*, by contrast, declined to resolve that issue because it found the relevant statutory text unambiguous. See 633 F.3d at 623.

As the government explained in *Grapevine*, see Gov't Br. 7-8, the various pending cases present the same two legal questions: (1) whether an understatement of gross income attributable to an overstatement of basis in sold property is an "omi[ssion] from gross income" within the meaning of Section 6501(e)(1)(A); and (2) to the extent that the statutory text is ambiguous, whether a recently issued Treasury regulation reasonably resolves that ambiguity. Compare Pet., *Beard*, *supra*, at i (presenting those two questions), and Pet., *Grapevine*, *supra*, at i (same), with Pet. I (same).

If the Court grants certiorari in either *Beard*, *Grapevine*, or this case, it will be called upon to answer those legal questions by applying the familiar two-step methodology set forth in *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837, 842-843 (1984). Although the Seventh Circuit in *Beard* (unlike the Federal Circuit in *Grapevine* or the court below) found it unnecessary to proceed to the second step of *Chevron* analysis, see 633 F.3d at 623, that aspect of the Seventh Circuit's analysis would not compromise this Court's ability to review both issues if

that becomes necessary. If this Court grants certiorari in *Beard* and ultimately finds the statutory language to be unclear, it can go on to determine whether the Treasury regulation validly resolves the ambiguity. And in making that determination, the Court can, of course, consult the decisions of those courts of appeals that have addressed the validity of the regulation.

Because *Beard* fully presents both questions and is the first-filed petition, there is no reason to grant certiorari in this case instead. Indeed, this case appears on balance to be a less suitable vehicle than *Beard* because the transactions at issue here are quite complicated, involving multiple taxpayers, trusts, and transfers. See Pet. 4-5. Because the transactions at issue in *Beard* involve a single set of transfers by a single taxpayer, that case presents the legal questions in a clearer factual context. And although amicus was denied leave to file an amicus brief by the Seventh Circuit in *Beard* (Amicus Br. 5, 19), there is no evident obstacle to amicus's participation in the proceedings in this Court if the Court grants certiorari in *Beard*.

If the Court grants the petition in *Beard* and concludes that an overstatement of basis in sold property does trigger the extended six-year assessment period, then the administrative adjustments at issue in this case were timely and the court of appeals erred in holding otherwise. Accordingly, the Court should hold this petition pending the disposition of *Beard*, including any subsequent proceedings on the merits, and then dispose of the petition as appropriate in light of those decisions.

CONCLUSION

The petition for a writ of certiorari should be held pending the Court's final disposition of *Beard* v. *CIR*, petition for cert. pending, No. 10-1553 (filed June 23, 2011), and then disposed of as appropriate.

Respectfully submitted.

DONALD B. VERRILLI, JR.
Solicitor General

SEPTEMBER 2011

AMICUS CURIAE BRIEF

SEP 2 - 2011

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA,
Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF OF BAUSCH & LOMB INCORPORATED AS *AMICUS CURIAE* CONDITIONALLY SUPPORTING CERTIORARI

ROGER J. JONES
ANDREW R. ROBERSON
LATHAM & WATKINS LLP
233 South Wacker Dr.
Suite 5800
Chicago, IL 60606

GREGORY G. GARRE
Counsel of Record
J. SCOTT BALLENGER
LATHAM & WATKINS LLP
555 11th Street, NW
Suite 1000
Washington, DC 20004
(202) 637-2207
gregory.garre@lw.com

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

INTEREST OF *AMICUS CURIAE* 1

INTRODUCTION AND SUMMARY OF ARGUMENT 3

ARGUMENT 6

I. THE COMMISSIONER'S READING OF 26 U.S.C. § 6501 IS IMPLAUSIBLE 6

II. THE SEVENTH CIRCUIT'S FAILURE TO REACH THE REGULATIONS IS A MATERIAL VEHICLE DEFICIENCY 13

III. THIS CASE PRESENTS A SUPERIOR VEHICLE TO *BEARD* TO DECIDE THE QUESTIONS PRESENTED 18

CONCLUSION 21

ADDENDUM

26 U.S.C. § 275 (1940) 1a

26 U.S.C. § 6229(c)(2) (1982) 2a

26 U.S.C. § 6501(e)(1)(A) (2006) 3a

TABLE OF AUTHORITIES

Page(s)

CASES

Bakersfield Energy Partners, LP v. CIR,
568 F.3d 767 (9th Cir. 2009) 9, 10, 11

Beard v. CIR,
633 F.3d 616 (7th Cir. 2011) ..... *passim*

Bowen v. Georgetown University Hospital,
488 U.S. 204 (1988) 17

Burks v. United States,
633 F.3d 347 (5th Cir. 2011) 9, 11, 17

Chevron U.S.A. Inc. v. NRDC,
467 U.S. 837 (1984) 16

Chock Full O' Nuts Corp. v. United States,
453 F.2d 300 (2d Cir. 1971) 17

Colony, Inc. v. CIR,
357 U.S. 28 (1958) 2, 7, 15, 16

Grapevine Importations, Ltd. v. United States,
636 F.3d 1368 (Fed. Cir. 2011) 11, 14

Home Concrete & Supply, L.L.C. v. United States,
634 F.3d 249 (4th Cir. 2011) 11, 15, 18

TABLE OF AUTHORITIES—Continued

Page(s)

Intermountain Insurance Service of Vail v. CIR,
No. 10-1204, 2011 WL 2451011 (D.C. Cir. June 21, 2011) 2, 10, 11, 17

Intermountain Insurance Service of Vail, LLC v. CIR,
134 T.C. 211 (2010), *rev'd*, 2011 WL 2451011 (D.C. Cir. June 21, 2011) 15, 17

Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA,
130 S. Ct. 1605 (2010) 12

Lorillard v. Pons,
434 U.S. 575 (1978) 12

NCAA v. Smith,
525 U.S. 459 (1999) 18

Phinney v. Chambers,
392 F.2d 680 (5th Cir.), *cert. denied*, 391 U.S. 935 (1968) 9

Russello v. United States,
464 U.S. 16 (1983) 13

Salman Ranch, Ltd. v. CIR,
No. 09-9015, 2011 WL 2120044 (10th Cir. May 31, 2011) 11

TABLE OF AUTHORITIES—Continued

Page(s)

Salman Ranch Ltd. v. United States,
573 F.3d 1362 (Fed. Cir. 2009) 8, 10, 11

United States v. Morton,
467 U.S. 822 (1984) 17

STATUTES AND REGULATIONS

26 U.S.C. § 6229(c)(2) 1, 12

26 U.S.C. § 6229(d)(1) 14

26 U.S.C. § 6501(e)(1)(A) ..... *passim*

26 U.S.C. § 7805(a) 4

26 U.S.C. § 7805 (note) 16

75 Fed. Reg. 78,897 (Dec. 17, 2010) 14

Treas. Reg. § 301.6299(c)(2)-1(b) (2010) 14

Treas. Reg. § 301.6501(e)-1(e) (2010) 14

OTHER AUTHORITIES

Black's Law Dictionary (7th ed. 1999) 8

H.R. Rep. No. 104-506, at 44 (1996), *reprinted in*
1996 U.S.C.C.A.N. 1143 16

TABLE OF AUTHORITIES—Continued

Page(s)

Pub. L. No. 104-168, 110 Stat. 1452 (1996) 16

T.D. 9511, 2011-6 I.R.B. 455 17

Webster's Third New International Dictionary (1969) 8

INTEREST OF *AMICUS CURIAE*

Bausch & Lomb Incorporated ("B&L") is an eye health company. Founded in 1853, it is one of the oldest, best known, and most respected healthcare brands.[1] This case is one of several currently pending before this Court, or soon to arrive, that present a circuit split concerning a complex set of statutory and administrative law issues relating to whether an overstatement of basis results in an omission from gross income that triggers the special statute of limitations under 26 U.S.C. § 6501(e)(1)(A). B&L has both a substantial interest in the issues presented by these cases and a unique perspective on the potential breadth of the Commissioner's arguments.

B&L is litigating a case in the Second Circuit in which—even though the case indisputably solely turns on the different statute of limitations set forth in 26 U.S.C. § 6229(c)(2), and not § 6501(e)(1)(A)—the Commissioner is making the same arguments as those presented in this case. *See Wilmington Partners v. CIR*, No. 10-4183 (2d Cir. filed Oct. 13, 2010). In addition, B&L also can provide a comprehensive view of the state of the law because it has filed *amicus* briefs in the Fourth, Fifth, Tenth, Federal, and D.C. Circuits on the same issues presented here. The courts of

---

[1] Pursuant to Supreme Court Rule 37.6, *amicus* states that no counsel for a party authored this brief in whole or in part; and no such counsel or any party made a monetary contribution intended to fund the preparation or submission of this brief. No person or entity, other than the *amicus* and its counsel, made a monetary contribution intended to fund the preparation and submission of this brief. Counsel of record for all parties have consented to the filing of this brief. Letters of consent from the appropriate counsel have been submitted to the Clerk concurrently with this filing.

appeals have recognized and relied upon those briefs. *See, e.g., Intermountain Ins. Serv. of Vail v. CIR*, No. 10-1204, 2011 WL 2451011, at *1 (D.C. Cir. June 21, 2011).

B&L's case (*Wilmington Partners*) underscores the potential implications of the government's position in these cases. The underlying transaction in *Wilmington Partners* does not involve a marketed tax shelter or so-called "listed transaction." Instead, the tax issues arise from unrelated good faith business restructurings driven by changing business realities and separated in time by more than six years. *See id.* at *6 (recognizing that B&L's case involves no "tax shelter allegation"). Moreover, as noted, the operative limitations period in *Wilmington Partners* is supplied by § 6229(c)(2)—and not § 6501(e)(1)(A). The Commissioner contends that two subparagraphs in § 6501(e)(1)(A) change the meaning of the language interpreted by this Court in *Colony, Inc. v. CIR*, 357 U.S. 28 (1958), (which is repeated verbatim in § 6501(e)(1)(A)). But § 6229(c)(2) does not contain those subparagraphs. It is phrased in *exactly* the same way as the statute interpreted in *Colony*, and was enacted against the backdrop of the *Colony* decision. Nonetheless, in *Wilmington Partners* the Commissioner has taken the remarkable position that the entirely different text and history of § 6229(c)(2) does not matter and is making the same § 6501(e)(1)(A)-based arguments that he has pressed in this case, and is claiming the same extraordinary and retroactive regulatory authority. The Commissioner is, in other words, pushing a position that is even more starkly inconsistent with this Court's clear holding in *Colony*.

Because the statute-of-limitations issue in *Wilmington Partners* indisputably solely turns on § 6229(c)(2)—and not § 6501(e)(1)(A)—there is no need for the Second Circuit in *Wilmington Partners* to delve into the complex issues presented in this case surrounding § 6501(e)(1)(A). *Wilmington Partners* can and should be decided based on a straightforward application of § 6229(c)(2), without even having to reach any question concerning § 6501(e)(1)(A). But since the Commissioner's arguments have consistently (and erroneously) conflated the two, B&L has been left with no choice but to participate in the § 6501 cases and explain why the Commissioner's interpretation of § 6501(e)(1)(A) is wrong and unsustainable on its own.

INTRODUCTION AND SUMMARY OF ARGUMENT

The United States claims that this case "presents the question whether an understatement of gross income attributable to an overstatement of basis in sold property is an 'omi[ssion] from gross income' that can trigger the six-year assessment period in 26 U.S.C. 6501(e)(1)(A)." Pet. 7. According to the government, "[t]hat question" is currently presented by the petition in *Beard v. CIR*, No. 10-1553 (filed June 23, 2011), and "*Beard* is the earlier-filed petition, and the government is not aware of any reason why this case would present a more suitable opportunity than *Beard* for resolving the circuit conflict." *Id.*

If this Court believes that certiorari is warranted to resolve the circuit conflict, there is sound reason why this case is "a more suitable opportunity than *Beard* for resolving the circuit conflict." The Commissioner's extraordinary efforts to rewrite the meaning of the operative tax provisions and overturn a decision of this

Court raise a number of interrelated issues. Even the government acknowledges at least two separate Questions Presented, Petition at (I), and the issues could easily be stated in a way that recognizes five or six other distinct, and important, issues. For example:

- Did this Court resolve the meaning of § 6501(e)(1)(A) in *Colony*?
- Does *Colony* recognize or leave any "ambiguity" that might permit the Commissioner to issue regulations overruling this Court's decision?
- Do the Treasury Regulations issued last year apply, by their terms, retroactively to reopen limitations periods that had already expired?
- Can the regulations apply retroactively to reopen limitations periods that had expired under existing law without exceeding the Commissioner's power under 26 U.S.C. § 7805(a)?
- Are the regulations entitled to deference under basic administrative law principles, given that they were promulgated in the midst of litigation in order to reverse the outcomes of legal contests that the Commissioner was losing?

In answering those questions, this Court should reject the government's arguments about the proper reading of § 6501(e)(1)(A). This Court rejected essentially the same arguments in *Colony* when interpreting a nearly identical predecessor statute. And to date the Seventh Circuit's decision in *Beard v. CIR*, 633 F.3d 616 (7th Cir. 2011), is the *only* court of appeals decision to conclude that a subparagraph added to § 6501(e)(1)(A) to clarify the definition of "gross

income" in a particular context alters the meaning of the general language that Congress reenacted when it passed § 6501(e)(1)(A), such that the new subparagraph requires a different conclusion than the one this Court reached in *Colony* (even though the language that this Court interpreted in *Colony* is the same). The *Beard* decision, which is wrong on its own terms, is thus an outlier. The other courts that have addressed these issues have focused on whether the 2010 regulations can or do change the proper interpretation of § 6501(e)(1)(A)—a question that *Beard*, alone among the pending decisions, simply declined to reach on the merits (and discussed only in passing in dictum). And while the issues surrounding the 2010 regulations were pressed by the taxpayer in *Beard*, they were not briefed as fully as in the other pending cases—in part because the Seventh Circuit, again alone among the courts of appeals, declined to accept the timely *amicus* brief that B&L presented in *Beard*.

The validity of the Commissioner's 2010 regulations attempting to change the meaning of settled statutory law and override a decision of this Court is a crux of the dispute presented by these cases. *Beard* presents a *potential* vehicle for certiorari on the questions presented in these cases. But if the Court believes that these questions warrant certiorari, it would be better served by considering the validity of the regulations in a case in which they have actually been passed on below, consistent with this Court's usual and settled practice of reserving certiorari for issues that were pressed and passed on below. The questions presented were actually decided by the Fourth Circuit below and this case is the most suitable vehicle for this Court's

review among the crop of cases currently pending before this Court on certiorari.

ARGUMENT

I. THE COMMISSIONER'S READING OF 26 U.S.C. § 6501 IS IMPLAUSIBLE

For decades in the wake of this Court's decision in *Colony*, the meaning of § 6501(e)(1)(A) was settled: an overstatement of tax basis does *not* result in an omission from gross income triggering the special statute of limitations established by that provision. A few years ago, in connection with the advent of the so-called "Son of BOSS" transaction, the Commissioner suddenly had a revelation: the operative language in § 6501(e)(1)(A) did not mean what this Court held in *Colony* and everyone—including the IRS—had understood for decades. The government has made an elaborate and implausible attempt to defend the Commissioner's new interpretation that an overstatement of basis *does* result in an "omi[ssion] from gross income," even when the return includes the sales price, basis, or other information. 26 U.S.C. § 6501(e)(1)(A); *Beard v. CIR*, No. 10-1553, Br. for Respondent at 8-11 (filed July 27, 2011) ("*Beard* Resp. Br."). That argument relies on the general definition of "gross income," a heavy emphasis on the word "amount," and an utter disregard of the ordinary meaning of the key word "omits." *Beard* Resp. Br. at 8-11; *see also Beard v. CIR*, 633 F.3d 616, 621-22 (7th Cir. 2011). It is precisely the same argument that this Court unequivocally rejected in *Colony*, when interpreting the identical "omits from gross income" language in the old § 275(c) of the 1939 Code.

The government also argues that two features of § 6501(e)(1)(A)—subparagraphs that by their terms do

not purport to address the meaning of the key phrase "omits from gross income"—"reinforce that understanding." *Beard* Resp. Br. at 11-13. Since this Court's decision in *Colony* is, of course, authoritative on the statutory language it construed, the government must mean that these new features of § 6501(e)(1)(A) *change* the statutory meaning of "omits from gross income" so dramatically as to overwhelm all the considerations that this Court discussed in *Colony* and require the opposite result, even though Congress did not change the operative language that was the basis for the Court's holding in *Colony*.

The heart of the government's argument, and the Seventh Circuit's holding in the *Beard* case, is that § 6501(e)(1)(A)(i) now provides that for "trade or business" taxpayers "the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services . . . prior to diminution by the cost of such sales or services." *Id.* at 11. The government contends that this provision, within its scope, ensures that an overstatement of the cost of goods sold could not constitute an omission from gross income, and argues that it "would be superfluous, or at least of extremely limited scope, if the general rule were that an overstatement of basis cannot give rise to an omission from gross income." *Id.* at 12. That argument has several glaring flaws.

First, that provision was already on the books when this Court decided *Colony*, and this Court closed its opinion by noting that its reasoning was *consistent* with the language of the new § 6501. *Colony, Inc. v. CIR*, 357 U.S. 23, 37 (1958). The Seventh Circuit rationalized that problem by suggesting that this Court meant that § 275(c) and the new § 6501(e)(1)(A)(i) were

consistent *on the facts of Colony* only because *Colony* itself supposedly involved "an omission of an actual receipt or accrual in a trade or business situation," and because the new § 6501(e)(1)(A)(ii) provides an adequate disclosure defense that accommodates some of the policy considerations that influenced this Court's reasoning in *Colony*. *Beard*, 633 F.3d at 620-21. "In other words," the Seventh Circuit reasoned that "*Colony*'s holding is inherently qualified by the facts of the case before the Court ...." *Id.* at 620. That reasoning collapses upon even the slightest scrutiny of *Colony*.

One problem with that reasoning is that the taxpayer in *Colony*, while perhaps a "trade or business," was not dealing in "goods or services" at all but in *land*.[2] More importantly, absolutely nothing in this Court's opinion suggests that this Court paid any attention to the taxpayer's line of business, or thought that it mattered in interpreting the statute before it. This Court's reasoning was based on the plain meaning of the language "omits from gross income," the legislative history of § 275(c), and the bizarre and anomalous consequences of the government's reading. None of those points were, or are, affected by the nature of the taxpayer's business. *See, e.g.*, *Salman Ranch Ltd. v. United States*, 573 F.3d 1362, 1372 (Fed. Cir. 2009) ("*Salman Ranch I*") ("We do not discern any

---

[2] The Code does not define "goods," but the ordinary meaning of the term, embraced by the Commissioner in *Salman Ranch*, is limited to movable personal property. *See Salman Ranch Ltd. v. United States*, No. 2008-5053, Brief for the Appellee, 2008 WL 4133498 (Fed. Cir. June 25, 2008) (citing *Black's Law Dictionary* 701 (7th ed. 1999); *Webster's Third New Int'l Dictionary* 978 (1969)).

basis for limiting *Colony*'s holding concerning the 'omits from gross income' language of I.R.C. § 275(c) to sales of goods or services by a trade or business. Neither the language nor rationale of *Colony* indicates such an intent on the part of the Court."); *Bakersfield Energy Partners, LP v. CIR*, 568 F.3d 767, 778 (9th Cir. 2009) (*Colony* "did not even hint that its interpretation of § 275(c) was limited to cases in which the taxpayer was engaged in a 'trade or business.'").

And while this Court did support its interpretation of "omits from gross income" by noting Congress's intent to confine the extended limitations period to situations in which the IRS is at a special disadvantage in detecting the issue, the Court in no way suggested that that language could have an entirely different meaning in the new § 6501(e)(1)(A) just because Congress added an explicit safe harbor for taxpayers who provided adequate disclosure. The Seventh Circuit believed that its interpretation was supported by the Fifth Circuit's decision in *Phinney v. Chambers*, 392 F.2d 680 (5th Cir.), *cert. denied*, 391 U.S. 935 (1968). *See Beard*, 633 F.3d at 620-21. But the Fifth Circuit has since expressly repudiated the Seventh Circuit's misreading of Fifth Circuit precedent. *See Burks v. United States*, 633 F.3d 347, 352 n.5 (5th Cir. 2011) ("The Seventh Circuit in *Beard* incorrectly read our decision in *Phinney* as limiting *Colony*'s holding.").

Second, as several other courts of appeals have explained, there is no genuine argument that this Court's interpretation of the "omits from gross income" language in *Colony* renders § 6501(e)(1)(A)(i) superfluous. Even accepting *Colony*, that subparagraph plays an important computational role in determining whether any omission affects 25% of the

taxpayer's gross income, by specifying (unlike the *Colony* holding) that cost of goods sold must be excluded from the denominator of the calculation in addition to the numerator. *See, e.g., Bakersfield*, 568 F.3d at 776 ("[W]e are not convinced that applying *Colony* to the 1954 Code would render § 6501(e)(1)(A)(i) superfluous," because "*Colony*'s holding . . . affects only" the numerator of gross income omitted "by defining what constitutes an omission from gross income."); *Salman Ranch I*, 573 F.3d at 1375 ("We do not see how [*Colony*'s] reading of the statutory language renders subparagraph (i) superfluous . . . .").

Indeed, even the Seventh Circuit did not genuinely advance an argument that § 6501(e)(1)(A) would be superfluous if *Colony* applied. Its reasoning is that "the special definition in subparagraph (i) would be, if not superfluous, certainly diminished." *Beard*, 633 F.3d at 622; *see also id.* at 623 ("To say that subsection (i) was included simply to clarify the 25% calculation diminishes the plain meaning of the statute."); *Intermountain Ins. Serv. of Vail v. CIR*, No. 10-1204, 2011 WL 2451011, at *11 (D.C. Cir. June 21, 2011) (acknowledging that the taxpayer's "point is well taken" and that the taxpayer "is technically correct that its interpretation avoids turning subsection (i) into surplusage"). But there is not, and could not be, any canon of construction against interpretations that "diminish" the potential scope of operation of a provision, while leaving it an important and meaningful role. The Seventh Circuit is merely saying, in a peculiar way, that a faithful application of this Court's holding in *Colony* would render § 6501(e)(1)(A)(i) less consequential than the Seventh Circuit believes it

should be. That *ipse dixit* reasoning has no grounding in ordinary canons of construction.

The government's statutory argument has not persuaded any court of appeals but the Seventh Circuit. The Fourth, Fifth, Ninth, and Federal Circuits have all ruled for the taxpayers on this issue. *See Home Concrete & Supply, L.L.C. v. United States*, 634 F.3d 249 (4th Cir. 2011); *Burks*, 633 F.3d 347 (5th Cir. 2011); *Bakersfield*, 568 F.3d 767 (9th Cir. 2009); *Salman Ranch I*, 573 F.3d 1362 (Fed. Cir. 2009). The Federal Circuit and Tenth Circuit have subsequently joined the government's camp, but only because they concluded that the 2010 regulations were applicable, valid, and *changed* the law. *See Grapevine Imps., Ltd. v. United States*, 636 F.3d 1368 (Fed. Cir. 2011); *Salman Ranch, Ltd. v. CIR*, No. 09-9015, 2011 WL 2120044 (10th Cir. May 31, 2011) ("*Salman Ranch II*"). The D.C. Circuit similarly relied on the regulations and held only that "nothing in section 6501(e)(1)(A) unambiguously forecloses the Commissioner from interpreting 'omissions from gross income' as including basis overstatements." *Intermountain*, 2011 WL 2451011, at *12.

For these reasons, *Beard* represents an unsound and ill-founded aberration when it comes to the proper interpretation of § 6501(e)(1)(A). The Seventh Circuit's erroneous decision in *Beard* deserves to be set aside, but that does not mean it presents the most suitable vehicle for this Court to resolve the questions presented in these cases.[3]

---

[3] As noted above, the applicable statute of limitations in *Wilmington Partners* is 26 U.S.C. § 6229(c)(2), not § 6501(e)(1)(A). Section 6501(e)(1)(A) applies when a *partner* has omitted from gross income an amount exceeding 25% of the gross income stated in the *partner's* return. By contrast, § 6229(c)(2) applies at the partnership level, and extends the limitations period to six years when the *partnership* omits from gross income an amount in excess of 25% of the *partnership's* gross income. The distinction is critical given the Commissioner's litigating position on the meaning of § 6501(e)(1)(A), because § 6229(c)(2) does not contain the subparagraphs (§ 6501(e)(1)(A)(i) and (ii)) at the heart of the Commissioner's argument in § 6501(e)(1)(A) cases. Instead, § 6229(c)(2) uses the *exact* same language as the old § 275(c) that this Court interpreted in *Colony*. When Congress enacted § 6229(c)(2) in 1982 the meaning of that language had been conclusively settled by *Colony*, and the unassailable conclusion is that when Congress enacted § 6229(c)(2) it therefore intended to adopt the meaning settled by *Colony*. *See Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA*, 130 S. Ct. 1605, 1616 (2010) ("We have often observed that when 'judicial interpretations have settled the meaning of an existing statutory provision, repetition of the same language in a new statute indicates, as a general matter, the intent to incorporate its ... judicial interpretations as well.'") (alteration in original) (citation omitted); *Lorillard v. Pons*, 434 U.S. 575, 580-81 (1978) (same).

Even assuming, *arguendo*, that there is any room for debate as to § 6501(e)(1)(A), the meaning of § 6229(c)(2) is thus unambiguously controlled by the *Colony* holding that Congress acted against when it enacted § 6229(c)(2) in 1982. That conclusion is underscored by the fact that the Commissioner did not conceive of his argument that § 6501(e)(1)(A) called for a different result

II. THE SEVENTH CIRCUIT'S FAILURE TO REACH THE REGULATIONS IS A MATERIAL VEHICLE DEFICIENCY

The Seventh Circuit in *Beard* noted that "[b]ecause we find that *Colony* is not controlling, we need not reach" the applicability or validity of the 2010 regulation—although it offered the conclusory *dicta* that it "would have been inclined to grant the [regulations] *Chevron* deference." *Beard*, 633 F.3d at 623. The issues the Seventh Circuit elected not to reach are critically important in this case. Although the taxpayer in *Beard* did press arguments concerning the regulations, this Court would be better served by taking a case in which the lower court actually *passed on* the taxpayer's arguments. There are several problems with the regulations meriting review.

First, by their own terms, the regulations do not apply in the manner that the Commissioner has argued

---

than *Colony* until 2005 or so—decades after Congress passed § 6229(c)(2). In *Wilmington Partners*, the Commissioner has nevertheless contended that § 6229(c)(2) should be given the same interpretation as § 6501(e)(1)(A), with nothing more than an *ipse dixit* and counterintuitive argument that these different provisions must be interpreted the same way for the Commissioner. But the well-settled rule, of course, is that "Congress acts intentionally and purposely in the disparate inclusion or exclusion" of statutory language. *Russello v. United States*, 464 U.S. 16, 23 (1983) (citation omitted). And the problem for the Commissioner is that the more he tries to attach significance to the subparagraphs added by § 6501(e)(1)(A), the more significant it has to be that Congress did *not* include those subparagraphs in § 6229(c)(2). There is simply no way around that conclusion for the government when it comes to § 6229(c)(2), making *Wilmington Partners* a different and far easier case for the taxpayer than any of the cases involving the application of § 6501(e)(1)(A).

in court. The regulations state that they apply only "to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009." Treas. Reg. §§ 301.6501(e)-1(e), 301.6229(c)(2)-1(b) (2010). The plain language of that regulation directs attention to whether the limitations period "was" open in September 2009 and, in particular, focuses on whether the "period for assessing tax" "was open" at that time. Assuming the government's statutory argument, discussed above, is rejected, then as of September 24, 2009 the governing law was this Court's decision in *Colony*, the ordinary three-year limitations period applied and had long-since expired in all of these cases, and (as such) the period for assessing tax obviously *was not* "open" on or after September 24, 2009.

The government's counter-argument rests on language from the regulation's preamble from the Federal Register (artfully blended with the actual controlling text, *see Beard* Resp. Br. at 15), which offers the interpretation that a taxable year is "open" if it is the "subject of any case pending before any court of competent jurisdiction ... in which a decision had not become final." 75 Fed. Reg. 78,897, 78,898 (Dec. 17, 2010). Of course, in many senses a *case* remains open until the exhaustion of all appeals. But in any non-Orwellian legal parlance a *limitations period* that has expired prior to the institution of litigation remains expired. Otherwise, the government could never lose on statute of limitations grounds, by definition. The government's argument rests on a Code provision indicating that limitations periods are *tolled* by the filing of litigation "until the decision of the court becomes final." 26 U.S.C. § 6229(d)(1); *see Grapevine*,

636 F.3d at 1382-83. But the concept of tolling only applies to extend an *open* limitations period; it does not *reopen* a limitations period that has already closed before the case is filed. The Fourth Circuit correctly held in this case that the government's interpretation is "contrary to the clearly and unambiguously expressed intent of Congress and must fail." *Home Concrete*, 634 F.3d at 257. The Tax Court aptly called the government's position circular and derived from result-driven logic. *Intermountain Ins. Serv. of Vail, LLC v. CIR*, 134 T.C. 211, 219 (2010) (*en banc*), *rev'd*, 2011 WL 2451011 (D.C. Cir. June 21, 2011). No measure of agency deference can sustain an interpretation of a rule that conflicts with the rule's own text and creates such an anomalous result.

Second, even if the regulations did apply, they are potentially entitled to *Chevron* deference only if there is an ambiguity for the agency to resolve. For most of the courts of appeals to consider these cases, therefore, the central issue has been whether this Court's decision in *Colony* leaves open the possibility that the government's arguments might constitute a *reasonable* interpretation of the statute, even though this Court firmly rejected them. As Judge Wilkinson explained in his thoughtful concurring opinion in this case, "*Colony* was decided under *Chevron* step one." *Home Concrete*, 634 F.3d at 258 (Wilkinson, J., concurring). This Court's opinion in *Colony* acknowledges a superficial textual ambiguity at the initial step of the analysis, but it held that resort to the conventional tools of statutory interpretation (including legislative history) *resolved* that ambiguity and that and the government's interpretation would create a "patent incongruity in the tax laws." *Colony*, 357 U.S. at 36-37.

This Court came to a firm conviction about when "Congress intended an exception to the usual three-year statute of limitations" and when it did not. *Id.* at 36. "If a court, employing traditional tools of statutory construction, ascertains that Congress had an intention on the precise question at issue, that intention is the law and must be given effect." *Chevron U.S.A. Inc. v. NRDC*, 467 U.S. 837, 843 n.9 (1984). *Colony* expressed such a conclusion as clearly as one could hope in a decision rendered more than two decades before *Chevron*. Indeed, Justice Harlan had the remarkable foresight to observe—in language that closely tracks the "precise question at issue" language that this Court used decades later in describing *Chevron* step one—that Congress had "address[ed] itself to the *specific situation*" at issue. *Colony*, 357 U.S. at 33 (emphasis added).

Third, even if the regulation applies and even if there is ambiguity to interpret, there are very serious questions about whether this regulation is valid and entitled to deference. Congress generally eliminated the Commissioner's authority to promulgate retroactive tax regulations in 1996,[4] and the

---

[4] *See* Pub. L. No. 104-168, § 1101(b), 110 Stat. 1452, 1469 (1996). That amendment effectuates Congress's longstanding intent that "it is generally inappropriate for Treasury to issue retroactive regulations." H.R. Rep. No. 104-506, at 44 (1996), *reprinted in* 1996 U.S.C.C.A.N. 1143, 1167. The text somewhat confusingly states that it "shall apply with respect to regulations that relate to statutory provisions enacted on or after the date of enactment." Pub. L. No. 104-168, § 1101(b), 110 Stat. at 1469; 26 U.S.C. § 7805 (note). The government reads that language to mean that the prior version of § 7805(b) applies to all post-1996 regulations unless the underlying Code provision was enacted after July 30, 1996. That interpretation eviscerates Congress's stated intent.

government's claim that these regulations "are not retroactive" simply ignores the ordinary meaning of that term.[5] And the fact that the Commissioner promulgated these regulations in the midst of pending litigation, to effectively reverse judicial decisions that were running very strongly in the taxpayers' favor, raises very difficult questions under retroactivity doctrine, the Administrative Procedures Act, and the *Chevron* doctrine. "Deference to what appears to be nothing more than an agency's convenient litigating position" is "entirely inappropriate," *Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 213 (1988), even when that litigating position has been laundered through a hollow charade of notice and comment rulemaking. *See, e.g., Burks*, 633 F.3d at 360 n.9; *Chock Full O' Nuts Corp. v. United States*, 453 F.2d 300, 303 (2d Cir. 1971) ("[T]he Commissioner may not take advantage of his power to promulgate retroactive regulations during the course of a litigation for the purpose of providing himself with a defense based on the presumption of validity accorded to such regulations."); *Intermountain*, 134 T.C. at 238-48 (Halpern and Holmes, JJ., concurring in result). *But see Intermountain*, 2011 WL 2451011, at *15.

The government claims this extraordinary new authority based primarily on dicta in a footnote in *United States v. Morton*, 467 U.S. 822, 835 n.21 (1984). *See Beard* Resp. Br. at 15-16; *Intermountain*, 2011 WL 2451011, at *12. Judge Wilkinson debunked this theory

---

The statute has to be understood as governing all regulations enacted after July 30, 1996 if they relate to statutory provisions—as opposed to internal Treasury matters, where retroactivity is permitted.

[5] T.D. 9511, 2011-6 I.R.B. 455.

as well. He wrote that "agencies are not a law unto themselves," and that the government's position in these cases "seems to me something of an inversion of the universe and to pass the point where the beneficial application of agency expertise gives way to a lack of accountability and a risk of arbitrariness." *Home Concrete*, 634 F.3d at 259 (Wilkinson, J., concurring).

III. THIS CASE PRESENTS A SUPERIOR VEHICLE TO *BEARD* TO DECIDE THE QUESTIONS PRESENTED

This Court has a strong and longstanding preference that all important issues in a case have been both pressed *and* passed on below. As this Court has observed, and as the Solicitor General himself is fond of reminding this Court, this Court ordinarily "do[es] not decide in the first instance issues not decided below." *NCAA v. Smith*, 525 U.S. 459, 470 (1999) (citations omitted); *see, e.g.*, *Teclezghi v. Holder*, No. 10-1210, Br. for Respondent in Opp'n, 2011 WL 2192271, at *19 (U.S. June 6, 2011) ("Specifically, the court of appeals did not address the question 'whether asylum seekers have the Fifth Amendment right to effective assistance of counsel' or 'what standard should be used to assess attorney performance.' This Court should not consider those questions in the first instance.") (citation omitted); *Hinkson v. United States*, No. 10-869, Br. for the U.S. in Opp'n, 2011 WL 805237, at *16 (U.S. Mar. 7, 2011) ("Neither the majority nor the dissenting judges on the court of appeals addressed that issue, and it would be a departure from the Court's normal practice to review it in the first instance."); *Sabhnani v. United States*, No. 10-476, Br. for the U.S. in Opp'n, 2010 WL 5102984, at *17-18 (U.S. Dec. 14, 2010) (stating that "[t]hat issue was not addressed in either of the lower

courts" and therefore "[t]here is no occasion for this Court to address that issue in the first instance"); *Ochoa v. Holder*, No. 09-1132, Br. for Respondent in Opp'n, 2010 WL 2502668, at *11 (U.S. June 18, 2010) ("Because this contention was ... [not] passed on below, this Court should not decide it in the first instance."); *Shabaz v. United States*, No. 09-636, Br. for the U.S. in Opp'n, 2010 WL 391258, at *6 (U.S. Feb. 1, 2010) (stating that "the court below did not address" the issue and therefore "[t]his Court should not review the question in the first instance"). There is no reason to break with the customary practice here, where there is a ready vehicle in which the issues *were* passed on.

Because the Seventh Circuit held that the best interpretation of § 6501(e)(1)(A) favors the Commissioner, it did not actually pass on the validity of the 2010 regulations or seriously delve into the significant issues surrounding those regulations. *See Beard*, 633 F.3d at 623. In addition, the Seventh Circuit, unlike every other court of appeals, denied B&L's timely motion for leave to participate as *amicus curiae*. As a result, the Seventh Circuit did not have before it certain arguments made in other cases and other arguments were not as fully developed as in the other pending cases. As B&L explained in a motion for reconsideration to the Seventh Circuit, B&L's *amicus* brief addressed additional legal issues not addressed in appellees' brief—including distinct arguments about *Chevron* deference, whether the temporary and final regulations were valid under the Administrative Procedures Act, and retroactivity. *Commissioner v. Beard*, No. 09-3741, Mot. for Reconsideration of Order Denying Mot. of Bausch & Lomb Inc. for Leave to File

Br. as *Amicus Curiae* in Supp. of Appellees and Affirmance at 3-4 (7th Cir. filed Aug. 3, 2010).

In this case, by contrast, the issues were fully briefed and the Fourth Circuit considered and actually passed on *both* the threshold *Colony* issue and the Commissioner's arguments based on the 2010 regulations. Respondents filed their brief in opposition early so that this case could be considered at the same Conference as *Beard*. And this case is a better vehicle than the other cases likely to arrive at this Court soon. Petitions also are pending in *Burks* and *Grapevine*. *Burks*, however, involves two separate consolidated cases—which could needlessly complicate the briefing. And, because the Federal Circuit had resolved the threshold statutory issue in favor of the taxpayers in *Salman Ranch I*, the *Grapevine* opinion focuses on the issues relating to the 2010 regulations.[6]

The Fourth Circuit's decision in this case—which includes a separate concurring opinion by Judge Wilkinson—considered the issues that will likely occupy this Court's attention more thoroughly and thoughtfully than the Seventh Circuit's decision in *Beard*. The fact that the *Beard* petition was "earlier-filed," Pet. 7, is not in itself a sufficient reason to grant certiorari in that case when a better vehicle is right at hand.

---

[6] In addressing the 2010 regulations issue in *Grapevine*, the Federal Circuit reaffirmed its holding in *Salman Ranch I* that this Court's *Colony* holding applies to § 6501. Thus, in the absence of this case, *Grapevine* would still represent a better vehicle than *Beard* because the *Grapevine* court (unlike the Seventh Circuit in *Beard*) passed on both the statute and the regulations.

CONCLUSION

If the Court believes that the questions presented by this case and *Beard* warrant certiorari, the Court should grant certiorari in this case.

Respectfully submitted,

ROGER J. JONES
ANDREW R. ROBERSON
LATHAM & WATKINS LLP
233 South Wacker Dr.
Suite 5800
Chicago, IL 60606

GREGORY G. GARRE
Counsel of Record
J. SCOTT BALLENGER
LATHAM & WATKINS LLP
555 11th Street, NW
Suite 1000
Washington, DC 20004
(202) 637-2207
gregory.garre@lw.com

September 2, 2011

ADDENDUM

TABLE OF CONTENTS

Page

26 U.S.C. § 275 (1940) 1a

26 U.S.C. § 6229(c)(2) (1982) 2a

26 U.S.C. § 6501(e)(1)(A) (2000) 3a

26 U.S.C. § 275(c) (1940)

§ 275. Period of limitation upon assessment and collection.

Except as provided in section 276—

* * *

(c) Omission from gross income.

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

* * *

26 U.S.C. § 6229(c)(2) (1982)

§ 6229. Period of limitations for making assessments.

* * *

(c) Special rule in case of fraud, etc.

* * *

(2) Substantial omission of income

If any partnership omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in its return, subsection (a) shall be applied by substituting "6 years" for "3 years".

* * *

26 U.S.C. § 6501(e)(1)(A) (2000)

§ 6501. Limitations on assessment and collection.

* * *

(e) Substantial omission of items

Except as otherwise provided in subsection (c)—

(1) Income taxes

In case of any tax imposed by subtitle A—

(A) General rule

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item.

* * *

JOINT APPENDIX

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

JOINT APPENDIX

DONALD B. VERRILLI, JR.
Solicitor General
Department of Justice
Washington, D.C. 20530-0001
SupremeCtBriefs@usdoj.gov
(202) 514-2217

Counsel of Record
for Petitioner

RICHARD T. RICE
Womble Carlyle Sandridge & Rice PLLC
One West 4th Street
Winston-Salem, N.C. 27101
rrice@wcsr.com
(336) 721-3609

Counsel of Record
for Respondents

PETITION FOR A WRIT OF CERTIORARI FILED: AUG. 3, 2011
CERTIORARI GRANTED: SEPT. 27, 2011

TABLE OF CONTENTS

Page

Court of appeals docket entries 1
District court docket entries 9
Complaint (Dec. 4, 2006) 21
First amended answer (Feb. 26, 2007) 34
Jenkins & Gilchrist tax opinion (Jan. 31, 2000) 41
Notice of final partnership administrative adjustment (Sept. 7, 2006) 82
District court order (Mar. 9, 2009) 98
Deposition of Robert L. Pierce (Aug. 6, 2009) 113
Home Concrete & Supply, L.L.C.'s Form 1065 partnership tax return: 1999 tax year 124
Home Oil & Coal Co., Inc.'s Form 1120S tax return: 1999 tax year 152
Stephen R. and Rebecca R. Chandler's Form 1040: 1999 tax year 189
Robert L. and Susanne D. Pierce's Form 1040: 1999 tax year 217
Robert L. Pierce Trust A, Form 1041: 1999 tax year .. 274
Robert L. Pierce Trust B, Form 1041: 1999 tax year .. 288

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 09-2353

HOME CONCRETE & SUPPLY, LLC, ET AL., PLAINTIFF

v.

UNITED STATES OF AMERICA, DEFENDANT

DOCKET ENTRIES

DATE	DOCKET NUMBER	PROCEEDINGS
		* * * * *
3/23/10	18	BRIEF filed by Appellants Rebecca R. Chandler, Stephen R. Chandler, Home Concrete & Supply, LLC, Home Oil and Coal Company, Incorporated, Robert L. Pierce and Susanne D. Pierce in electronic and paper format. Type of Brief: Opening. Method of Filing Paper Copies: hand delivery. Date Paper Copies Mailed, Dispatched, or Delivered to Court: 03/23/2010.. Is this a redacted brief? No. If yes, have you verified that

DATE	DOCKET NUMBER	PROCEEDINGS
		the redacted material cannot be revealed by cutting and pasting text? N/A. [998304482] [09-2353] Robert Numbers
		* * * * *
3/30/10	22	AMICUS CURIAE/INTERVENOR BRIEF filed by Jones, Roger J. Counsel for Amicus Curiae Bausch & Lomb Incorporated in electronic and paper format. Type of Brief: Amicus Curiae. Method of Filing Paper Copies: mail. Date Paper Copies Mailed, Dispatched, or Delivered to Court: 03/30/2010. [998309307] [09-2353] Roger Jones
		* * * * *
4/30/10	34	BRIEF filed by Appellee US in electronic and paper format. Type of Brief: Response. Method of Filing Paper Copies: mail. Date Paper Copies Mailed, Dispatched, or Delivered to

DATE	DOCKET NUMBER	PROCEEDINGS
		Court: 04/30/2010.. Is this a redacted brief? No. If yes, have you verified that the redacted material cannot be revealed by cutting and pasting text? N/A. [998330482] [09-2353] Joan Oppenheimer
		* * * * *
6/1/10	36	BRIEF filed by Appellants Rebecca R. Chandler, Stephen R. Chandler, Home Concrete & Supply, LLC, Home Oil and Coal Company, Incorporated, Robert L. Pierce and Susanne D. Pierce in electronic and paper format. Type of Brief: Reply. Method of Filing Paper Copies: hand delivery. Date Paper Copies Mailed, Dispatched, or Delivered to Court: 06/01/2010.. Is this a redacted brief? No. If yes, have you verified that the redacted material cannot be revealed by cutting and pasting text? N/A. [998350567] [09-2353] Robert Numbers

DATE	DOCKET NUMBER	PROCEEDINGS
		* * * * *
10/7/10	42	SUPPLEMENTAL AUTHORITIES (FRAP 280(j)) filed by Appellee US. [998442022]. [09-2353] Joan Oppenheimer
10/13/10	43	Letter filed re: [42]. Supplemental Authorities filed by Appellants Rebecca R. Chandler, Stephen R. Chandler, Home Concrete & Supply, LLC, Home Oil and Coal Company, Incorporated, Robert L. Pierce and Susanne D. Pierce. [998444415] [09-2353] Robert Numbers
10/27/10	44	ORAL ARGUMENT heard before the Honorable J. HARVIE WILKINSON, III, ROGER L. GREGORY and JAMES A. WYNN, JR.. Attorneys arguing case: Mr. Richard Rice and Mr. Charles Mark Wiley for Appellants Home Concrete & Supply, LLC, Home Oil and Coal Company, Incorporated and Ms. Joan Iris Oppen-

DATE	DOCKET NUMBER	PROCEEDINGS
		heimer for Appellee US. Courtroom Deputy: Lisa Robertson. [998454573] [09-2353] (LER)
		* * * * *
12/15/10	47	SUPPLEMENTAL AUTHORITIES (FRAP 28(j)) filed by Appellee US. [998486060]. [09-2353] Joan Oppenheimer
12/22/10	48	SUPPLEMENTAL AUTHORITIES (FRAP 28(j)) response filed by Appellants Rebecca R. Chandler, Stephen R. Chandler, Home Concrete & Supply, LLC, Home Oil and Coal Company, Incorporated, Robert L. Pierce and Susanne D. Pierce. [998490418]. [09-2353] Robert Numbers
12/22/10	49	SUPPLEMENTAL AUTHORITIES (FRAP 28(j)) response filed by Amicus Supporting Appellant Bausch & Lomb, Inc..

DATE	DOCKET NUMBER	PROCEEDINGS
		[998490501]. [09-2353] Roger Jones
1/12/11	50	SUPPLEMENTAL AUTHORITIES (FRAP 28(j)) filed by Appellee US. [998501889]. [09-2353] Joan Oppenheimer
1/21/11	51	Letter filed re: [50], Supplemental Authorities filed by Appellants Rebecca R. Chandler, Stephen R. Chandler, Home Concrete & Supply, LLC, Home Oil and Coal Company, Incorporated, Robert L. Pierce and Susanne D. Pierce. [998507919] [09-2353] Richard Rice
1/26/11	52	SUPPLEMENTAL AUTHORITIES (FRAP 28(j)) filed by Appellee US. [998511428]. [09-2353] Joan Oppenheimer
1/31/11	53	Letter filed re: [52], Supplemental Authorities filed by Appellants Rebecca R. Chandler, Stephen R. Chandler, Home Concrete & Supply, LLC, Home Oil and Coal

DATE	DOCKET NUMBER	PROCEEDINGS
		Company, Incorporated, Robert L. Pierce and Susanne D. Pierce. [998514771] [09-2353] Robert Numbers
2/7/11	54	PUBLISHED AUTHORED OPINION filed. Originating case number: 7:06-cv-00181-FL Copies to all parties and the district court/agency. [998519282] [09-2353] (MR)
2/7/11	55	JUDGMENT ORDER filed. Disposition method: 09-2353 opn.p.arg. Decision: Reversed. Originating case number: 7:06-cv-00181-FL. Entered on Docket Date: 02/07/2011. [998519296] Copies to all parties and the district court/agency. [09-2353] (MR)
3/23/11	57	PETITION for rehearing en banc (FRAP 35) by Appellee US. [09-2353] Joan Oppenheimer

DATE	DOCKET NUMBER	PROCEEDINGS
3/23/11	58	Mandate stayed by FRAP 41(d)(1).. [09-2353] (JSN)
4/5/11	59	COURT ORDER filed [998560579] denying Motion for rehearing en banc [57] Copies to all parties . . . [09-2353] (JSN)
4/13/11	60	Mandate issued. Referencing: [55], Judgment order, [54], Published Authored Opinion. Originating case number: 7:06-cv-00181-FL.. [09-2353] (JSN)

* * * * *

UNITED STATES DISTRICT COURT FOR THE
EASTERN DISTRICT OF NORTH CAROLINA
SOUTHERN DIVISION

No. 7:06-CV-00181-FL

HOME CONCRETE & SUPPLY, LLC, ET AL., PLAINTIFF

v.

UNITED STATES OF AMERICA, DEFENDANT

DOCKET ENTRIES

DATE	DOCKET NUMBER	PROCEEDINGS
12/5/06	1	COMPLAINT *and Petition for Readjustment of Partnership Items Under 26 U.S.C. Section 6226* against UNITED STATES OF AMERICA (Filing fee $ 350 receipt number 10528495.), filed by Susanne D. Pierce, Home Concrete & Supply, LLC, Robert L. Pierce, Stephen R. Chandler, Rebecca R. Chandler, Home Oil and Coal Co., Inc.. (Attachments: # 1 Exhibit A) (Numbers, Robert) (Entered: 12/05/2006)

DATE	DOCKET NUMBER	PROCEEDINGS
		* * * * *
2/5/07	9	ANSWER to Complaint by UNITED STATES OF AMERICA. (Egan, Christopher) (Entered: 02/05/2007)
		* * * * *
12/12/07	45	MOTION for Partial Summary Judgment by UNITED STATES OF AMERICA. Responses due by 1/18/2008 (Egan, Christopher) (Entered: 12/12/2007)
12/12/07	46	Memorandum in Support re 45 MOTION for Partial Summary Judgment *Brief Supporting United States' Motion for Partial Summary Judgment* filed by UNITED STATES OF AMERICA. (Attachments: # 1 Declaration- Davis - IRS, #2 Declaration - Dorsey - J&G, # 3 Declaration - Schroder - AA, # 4 Exhibit 1, # 5 Exhibit 2, # 6 Exhibit 3, # 7 Exhibit 4, # 8 Exhibit 5, # 9 Exhibit 6, # 10 Exhibit 7, # 11 Exhibit

DATE	DOCKET NUMBER	PROCEEDINGS
		8, # 12 Exhibit 9, # 13 Exhibit 10, # 14 Exhibit 11, # 15 Exhibit 12, # 16 Exhibit 13, # 17 Exhibit 14, # 18 Exhibit 15, # 19 Exhibit 16, # 20 Exhibit 17, # 21 Exhibit 18, # 22 Exhibit 19, # 23 Exhibit 20, # 24 Exhibit 21, # 25 Exhibit 22, # 26 Errata 23, # 27 Exhibit 24, # 28 Exhibit 25) (Egan, Christopher) (Entered: 12/12/2007)
		* * * * *
12/12/07	52	MOTION for Summary Judgment by Susanne D. Pierce, Home Concrete & Supply, LLC, Robert L. Pierce, Stephen R. Chandler, Rebecca R. Chandler, Home Oil and Coal Co., Inc.. (Rice, Richard) (Entered: 12/12/2007)
12/12/07	53	Memorandum in Support re 52 MOTION for Summary Judgment filed by Susanne D. Pierce, Home Concrete & Supply, LLC, Robert L.

DATE	DOCKET NUMBER	PROCEEDINGS
		Pierce, Stephen R. Chandler, Rebecca R. Chandler, Home Oil and Coal Co., Inc.. (Attachments: # 1 Exhibit A, # 2 Exhibit B, # 3 Exhibit C (Part 1), # 4 Exhibit C (Part 2), # 5 Exhibit D, # 6 Exhibit E, # 7 Exhibit F, # 8 Exhibit G, # 9 Exhibit H, # 10 Exhibit I) (Rice, Richard) (Entered: 12/12/2007)
1/18/08	54	RESPONSE in Opposition re 52 MOTION for Summary Judgment filed by UNITED STATES OF AMERICA. (Egan, Christopher) (Entered: 01/18/2008)
1/18/08	55	RESPONSE to Motion re 45 MOTION for Partial Summary Judgment filed by Susanne D. Pierce, Home Concrete & Supply, LLC, Robert L. Pierce, Stephen R. Chandler, Rebecca R. Chandler, Home Oil and Coal Co., Inc.. (Attachments: # 1 Exhibit A) (Rice, Richard) (Entered: 01/18/2008)

DATE	DOCKET NUMBER	PROCEEDINGS
		* * * * *
11/21/08	59	ORDER re 45 Motion for Partial Summary Judgment and 52 Motion for Summary Judgment. Plaintiff's motion for summary judgment is denied in part, and in corresponding part, defendant's motion is allowed. The court holds in abeyance decision on remaining parts pending receipt and review of supplemental briefing herein ordered. The parties' supplemental memoranda, not to exceed 30 pages in length, shall be filed and served on or before December 22, 2008. Responses, not to exceed 15 pages in length, shall be filed and served on or before January 19, 2009. Signed by Chief Judge Louise Wood Flanagan on 11/21/08. Cys served electronically. (Baker, C.) (Entered: 11/21/2008)

DATE	DOCKET NUMBER	PROCEEDINGS
12/22/08	60	Plaintiffs' Supplemental Brief by Susanne D. Pierce, Home Concrete & Supply, LLC, Robert L. Pierce, Stephen R. Chandler, Rebecca R. Chandler, Home Oil and Coal Co., Inc.. (Attachments: # 1 Exhibit A - 754 Election Statement, # 2 Exhibit B - Form 8594, # 3 Exhibit C - Schedule D, # 4 Exhibit D - Partnership Tax Return, #5 Exhibit E - Initial Return, # 6 Exhibit F - Footnote (Pierce), # 7 Exhibit G - Footnote (Chandler), # 8 T.C. Memo 2000-286) (Rice, Richard) Modified on 12/29/2008 to terminate motion and correct docket entry text to reflect correct document title (Baker, C.). (Entered: 12/22/2008)
12/22/08	61	Memorandum in Support re 59 Order on Motion for Partial Summary Judgment,,, Order on Motion for Summary Judgment,, 45 MO-

DATE	DOCKET NUMBER	PROCEEDINGS
		TION for Partial Summary Judgment *Supplemental Briefing Supporting United States' Motion for Partial Summary Judgment* filed by UNITED STATES OF AMERICA. (Attachments: # 1 Chart A, # 2 Chart B, # 3 Burks v. United States) (Egan, Christopher) (Entered: 12/22/2008)
		* * * * *
1/19/09	63	RESPONSE re 62 Order, 60 Supplemental MOTION for Summary Judgment *Plaintiffs' Supplemental Brief*, 52 MOTION for Summary Judgment, 45 MOTION for Partial Summary Judgment, 61 Memorandum in Support, *United States' Response to Plaintiffs' Supplemental Briefing* filed by UNITED STATES OF AMERICA. (Egan, Christopher) (Entered: 01/19/2009)

DATE	DOCKET NUMBER	PROCEEDINGS
1/30/09	64	REPLY to Response to Motion re 52 MOTION for Summary Judgment filed by Susanne D. Pierce, Home Concrete & Supply, LLC, Robert L. Pierce, Stephen R. Chandler, Rebecca R. Chandler, Home Oil and Coal Co., Inc.. (Attachments: # 1 Exhibit A - Election Statement, # 2 Exhibit B - Election to Adjust Basis of Partnership Property,# 3 Exhibit C - Asset Acquisition Statement, # Exhibit D - Distribution, # 5 Exhibit E- Alex Brown Receipt) (Rice, Richard) (Entered: 01/30/2009)
		* * * * *
3/9/09	65	ORDER - The defendant's motion for partial summary judgment is GRANTED and the plaintiffs' motion for summary judgment is DENIED. Accordingly, pursuant to this court's previous order entered on October 9, 2007, the parties shall submit

DATE	DOCKET NUMBER	PROCEEDINGS
		a Joint Status Report by March 23, 2009, proposing an expeditious schedule for the conduct of any further discovery, and requested trial dates. If further settlement activities may prove beneficial, this information also shall be reported. A magistrate judge may be made available to facilitate a court-hosted settlement conference if requested. Signed by Chief Judge Louise Wood Flanagan on 03/09/09. Copies served electronically. (Baker, C.) (Entered: 03/09/2009)
		* * * * *
9/17/09	88	*SET ASIDE PURSUANT TO ORDER AT 89 * - ORDER - The court has been advised that the parties have settled all matters in controversy among them. Therefore, this matter is DISMISSED subject to the right

DATE	DOCKET NUMBER	PROCEEDINGS
		of any party to file a motion to reopen the case should settlement not be consummated within thirty (30) days hereof. The parties are directed to file their Stipulation of Dismissal With Prejudice on or before October 17, 2009. The Clerk of Court is directed to remove this matter from the court's pretrial and trial calendars. Signed by Chief Judge Louise Wood Flanagan on 09/17/09. Copies served electronically. (Baker, C.) Modified on 10/5/2009 (Baker, C.). (Entered: 09/17/2009)
9/21/09	89	ORDER- This matter comes now before the court of its own initiative, in furtherance of the parties' settlement efforts, culminating in a settlement reached in conference with the magistrate judge September 16, 2009, as reported to the court. In adherence to custom, upon said

DATE	DOCKET NUMBER	PROCEEDINGS
		report on September 17, 2009, the court entered order removing the case from its active docket. The court now is aware that dismissal effectuated therein has come before the parties have had opportunity to assemble and present certain documents necessary to consummate their settlement on the agreed to terms reached at court-hosted settlement conference. The court sets aside the September 17, 2009 Order 88, and in further of their settlement, the parties shall file a proposed consent judgment, or such other appropriate documents necessary to consummate settlement and fully conclude the case in the district court, on or before October 5, 2009. Signed by Chief Judge Louise Wood Flanagan on 09/21/09. Copies served electronically. (Baker, C.) Modified on 10/2/2009 (Baker, C.). (Entered: 09/21/2009)

DATE	DOCKET NUMBER	PROCEEDINGS
		* * * * *
10/6/09	91	FINAL JUDGMENT - Signed by Chief Judge Louise Wood Flanagan on 10/06/09. Copies served electronically. (Baker, C.) (Entered: 10/06/2009)
12/4/09	92	NOTICE OF APPEAL as to 65 Order, 38 Order on Motion for Judgment on the Pleadings, 59 Order on Motion for Partial Summary Judgment, Order on Motion for Summary Judgment, 91 Consent Judgment by Susanne D. Pierce, Home Concrete & Supply, LLC, Robert L. Pierce, Stephen R. Chandler, Rebecca R. Chandler, Home Oil and Coal Co., Inc. Filing fee $ 455, receipt number 0417000000001043012. (Numbers, Robert) (Entered: 12/04/2009)
		* * * * *

UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA

Civil Action No.

HOME CONCRETE & SUPPLY, LLC, A DELAWARE LIMITED LIABILITY COMPANY; ROBERT L. PIERCE, AS TAX MATTERS PARTNER; SUSANNE D. PIERCE; STEPHEN R. CHANDLER; REBECCA R. CHANDLER; HOME OIL AND COAL COMPANY, INC., A NORTH CAROLINA CORPORATION, PLAINTIFFS/PETITIONERS

v.

UNITED STATES OF AMERICA, DEFENDANT/RESPONDENT

[Filed: Dec. 4, 2006]

COMPLAINT AND PETITION FOR READJUSTMENT OF PARTNERSHIP ITEMS UNDER 26 U.S.C. § 6226

Plaintiffs/Petitioners complaining of Defendant/Respondent allege:

INTRODUCTION

1. This is an action seeking a determination that any assessment of taxes, interest and penalties against Plaintiffs/Petitioners for the 1999 tax year is barred under the applicable statute of limitations. In the alterna-

tive, Plaintiffs/Petitioners seek a determination that no adjustment to their taxes is warranted for the 1999 tax year. In either case, Plaintiff/Petitioner Robert L. Pierce seeks reimbursement of $1,392,118.00, which he deposited with the Internal Revenue Service (the "Service") pursuant to Section 6226(e)(1) of the Internal Revenue Code, as amended (the "Code").

PARTIES

2. Plaintiff/Petitioner Home Concrete & Supply, LLC ("Home Concrete") is a Delaware limited liability company with its current principal place of business in Wilmington, New Hanover County, North Carolina. For state law purposes, Home Concrete is a limited liability company and its owners are referred to as "members." However, for federal income tax purposes, Home Concrete is a partnership and its owners are partners. Any reference to Home Concrete as a partnership, and any reference to Home Concrete's members as partners, refers to their status for federal income tax purposes.

3. Plaintiff/Petitioner Robert L. Pierce, the Tax Matters Partner of Home Concrete, resides in Wilmington, New Hanover County, North Carolina. For the 1999 federal income tax year, Robert Pierce timely filed his return jointly with his wife, Plaintiff/Petitioner Susanne D. Pierce.

4. Plaintiff/Petitioner Stephen R. Chandler was a partner of Home Concrete during the 1999 tax year and, therefore, is treated as a party to this action pursuant to Code § 6226(c). For the 1999 federal income tax year, Stephen Chandler timely filed his return jointly with his wife, Plaintiff/Petitioner Rebecca R. Chandler.

5. Plaintiff/Petitioner Home Oil and Coal Company, Inc., a North Carolina corporation ("Home Oil"), was a partner of Home Concrete during the 1999 tax year and, therefore, is treated as a party to this action pursuant to Code Section 6226(c).

6. Plaintiffs/Petitioners Robert Pierce (individually and as the owner of Trust A and Trust B (defined below)), Susanne Pierce, Stephen Chandler, Rebecca Chandler and Home Oil, collectively are referred to herein as the "Taxpayers."

7. Defendant/Respondent is the United States of America.

JURISDICTION AND VENUE

8. Plaintiffs/Petitioners incorporate paragraphs 1 through 7 as if fully set forth herein.

9. On September 7, 2006, the Commissioner (the "Commissioner") of the Service issued a Notice of Final Partnership Administrative Adjustment (the "FPAA") to Home Concrete for the tax year ended December 31, 1999.

10. The adjustments proposed in the FPAA would result in deficiencies for each of the individual Taxpayers because their taxable income, through their respective limited liability company or S corporation ownership interests, would be increased if the adjustments set forth in the FPAA were upheld.

11. This Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1346(e) and the Plaintiffs/Petitioners have standing to bring this Complaint and Petition pursuant to Code § 6226(a).

12. Venue is appropriate in the United States District Court for the Eastern District of North Carolina pursuant to Code § 6226(a).

13. Pursuant to Code § 6226(e)(1), prior to the filing of this Complaint and Petition, Plaintiff/Petitioner Robert Pierce, in his capacity as Tax Matters Partner of Home Concrete, deposited with the Service $1,392,118.00.

FACTS

14. Plaintiffs/Petitioners incorporate paragraphs 1 through 13 as if fully set forth herein.

Background

15. For the period from 1985 to 1999 Plaintiffs/Petitioners Robert Pierce and Stephen Chandler were the principal owners and day-to-day managers of Home Oil, a producer and distributor of ready-mix concrete and other building supplies, and on a limited basis, a distributor of residential heating oil.

16. In 1999, Plaintiffs/Petitioners Robert Pierce and Stephen Chandler decided to sell Home Oil and decrease their day-to-day involvement in the business of the company.

17. Plaintiffs/Petitioners Robert Pierce and Stephen Chandler, long-time operators of a concrete company without any significant background in the financial or tax matters associated with preparing a business for sale or selling a business, sought the advice, counsel and guidance of competent professional advisors to assist them in preparing for and completing the sale of Home Oil.

18. Plaintiffs/Petitioners Robert Pierce and Stephen Chandler first engaged the services of accounting firm Arthur Andersen LLP ("Andersen"). Then, representatives of Andersen recommended the additional engagement of the national law firm Jenkens & Gilchrist, P.C. ("Jenkens"). Plaintiffs/Petitioners also engaged a business broker, Lloyd & Company, and local counsel, Brooks, Pierce, McLendon, Humphrey & Leonard, L.L.P. The Taxpayers relied on their professional advisors to use their professional judgment to plan and document the reorganization and sale of Home Oil in a legally proper and financially sound manner.

19. Pursuant to the professional business and tax advice of these professional advisors regarding the sale of Home Oil, the following transactions occurred:

Formation of Entities

(a) Home Concrete was formed on April 15, 1999.

(b) Home Concrete's initial members were (i) Robert Pierce, (ii) Stephen Chandler, (iii) Home Oil, (iv) the 1999 Robert L. Pierce Grantor Trust U/A dated 4/21/99 Trust A FBO Julie Margaret Pierce ("Trust A"); and (v) The 1999 Robert L. Pierce Grantor Trust U/A dated 4/21/99 Trust B FBO Robert Craig Pierce ("Trust B").

(c) Salisbury Investments LLC ("Salisbury Investments") was formed on April 15, 1999. Salisbury Investments is a single member limited liability company owned by Robert Pierce.

(d) Goodnight Investments LLC ("Goodnight Investments") was formed on April 15, 1999. Goodnight Investments is a single member limited liability company owned by Stephen Chandler.

Short Sale of U.S. Treasury Notes

(e) On May 13, 1999, Robert Pierce, through Salisbury Investments, commenced a short sale in which he sold $60,000 face value Treasury Notes maturing January 31, 2001 for $60,090.80 plus interest of $896.27, for total proceeds equal to $60,987.07.

(f) On May 13, 1999, Stephen Chandler, through Goodnight Investments, commenced a short sale in which he sold $1.387 million face value Treasury Notes maturing January 31, 2001 for $1,389,164.25 plus interest of $20,718.79, for total proceeds equal to $1,409,883.04.

(g) On May 13, 1999, Robert Pierce, in his capacity as grantor of Trust A, commenced a short sale in which he sold through Trust A $2.952 million face value Treasury Notes maturing January 31, 2001 for $2,956,670.86 plus interest of $44,097.43, for total proceeds equal to $3,000,768.29.

(h) On May 13, 1999, Robert Pierce, in his capacity as grantor of Trust B, commenced a short sale in which he sold through Trust B $2.952 million face value Treasury Notes maturing January 31, 2001 for $2,956,670.86 plus interest of $44,097.43, for total proceeds equal to $3,000,768.29.

Contributions by the Taxpayers to the Capital of Home Concrete

(i) On May 17, 1999, Robert Pierce, through Salisbury Investments, transferred $60,987.07 (the proceeds from the short sale of Treasury Notes), together with the short Treasury Note position and $1,600.00 margin cash, to Home Concrete as a capital contribution.

(j) On May 17, 1999, Stephen Chandler, through Goodnight Investments, transferred $1,409,883.04 (the proceeds from the short sale of Treasury Notes), together with the short Treasury Note position and $30,400.00 margin cash, to Home Concrete as a capital contribution.

(k) On May 17, 1999, Robert Pierce, in his capacity as grantor of Trust A, transferred $3,000,768.29 (the proceeds from the short sale of Treasury Notes), together with the short Treasury Note position and $64,000.00 margin cash, to Home Concrete as a capital contribution.

(l) On May 17, 1999, Robert Pierce, in his capacity as grantor of Trust B, transferred $3,000,768.29 (the proceeds from the short sale of Treasury Notes), together with the short Treasury Note position and $64,000.00 margin cash, to Home Concretes as a capital contribution.

Close of Short Sale Position

(m) On May 18, 1999, Home Concrete covered its Treasury Note short position by paying $7,359,043.00, in the aggregate, to purchase Treasury Notes in the open market.

(n) As a result of the completed short sale, Home Concrete realized a short-term capital gain of $113,362.00 that was allocated to each of Home Concrete's partners in accordance with their respective percentage interests.

Contributions by Home Oil to the Capital of Home Concrete and Transfers of Membership Interests in Home Concrete

(o) On June 11, 1999, Home Oil transferred substantially all of its business assets to Home Concrete as a capital contribution.

(p) On June 14, 1999, Robert Pierce transferred a percentage of his membership interest in Home Concrete to Home Oil as a capital contribution to Home Oil.

(q) On June 14, 1999, Stephen Chandler transferred a percentage of his membership interest in Home Concrete to Home Oil as a capital contribution to Home Oil.

(r) On June 14, 1999, Robert Pierce, in his capacity as grantor of Trust A, transferred a percentage of Trust A's membership interest in Home Concrete to Home Oil as a capital contribution to Home Oil.

(s) On June 14, 1999, Robert Pierce, in his capacity as grantor of Trust B, transferred a percentage of Trust B's membership interest in Home Concrete to Home Oil as a capital contribution to Home Oil.

(t) At the time of the transfers described in paragraphs 19(p)-19(s) above, the only assets of Home Concrete were cash and the business assets contributed by Home Oil (see paragraph 19(o)).

Sale of Business Assets

(u) On August 31, 1999, Home Concrete sold substantially all of its assets to a third party purchaser for an aggregate purchase price of $10,623,348.00, resulting in gain to Home Concrete of $69,125.08.

Filing of Returns and Audit

20. Based on the information provided by their advisors, the Taxpayers at all times regarded the short sale of Treasury Notes and related transactions as investments carrying the potential for generating profits, independent of any tax benefits, and in fact the short sale resulted in a short term capital gain of $113,362.00.

21. Prior to the filing of the Taxpayers' respective income tax returns for the 1999 tax year, Jenkens provided to each individual Taxpayer a separate legal opinion dated January 31, 2000, which provided the bases for items of income, loss and deduction reported by the Taxpayers in their respective tax returns for the tax year ended December 31, 1999.

22. Home Concrete timely filed its Form 1065 Partnership Tax Return on or prior to April 17, 2000. The Home Concrete Return contained information relating to the transactions described in paragraph 19 above, including, among other items, a statement titled "Election to Adjust Basis of Partnership Property" (the "Election Document"). The Election Document contained a detailed calculation of the positive basis adjustment of $5,984,526.17 permitted by Code § 743(b) upon the making of an election under Code § 754. The Service contends that the Taxpayers are not entitled to the benefit of this positive basis adjustment.

23. A genuine copy of the Home Concrete Return is attached hereto as Exhibit A, which is incorporated herein by reference.

24. Home Oil timely filed its Form 1120S Income Tax Return for an S Corporation, which contained all

allocable items of income, loss and deduction from Home Concrete, on or before April 17, 2000.

25. Robert and Susanne Pierce timely filed their joint Form 1040 Individual Tax Return on or before April 17, 2000, which contained all allocable items of income, loss and deduction from Home Concrete and Home Oil, including items allocable to Trust A and Trust B pursuant to the grantor trust rules of Subtitle A, Chapter 1, Subchapter J of the Code.

26. Stephen and Rebecca Chandler timely filed their joint Form 1040 Individual Income Tax Return on or before April 17, 2000, which contained all allocable items of income, loss and deduction from Home Concrete and Home Oil.

27. Under Code §§ 6229 and 6501, the period of limitations for assessment applicable to Home Concrete for the 1999 tax year expired April 17, 2003. No assessment was made on or before April 17, 2003.

28. Under Code § 6501, the period of limitations for assessment applicable to Plaintiffs/Petitioners Robert and Susanne Pierce and Stephen and Rebecca Chandler for the 1999 tax year expired April 17, 2003. No assessment was made on or before April 17, 2003.

29. Under Code § 6501, the period of limitations for assessment applicable to Home Oil for the 1999 tax year expired three years after the filing date of the Home Oil Return. No assessment was made on or before the third anniversary of such filing.

30. On May 17, 2004, the Service obtained the Taxpayers' names through a client list provided to the Service by Jenkens, and thereafter reviewed the Taxpayers'

federal income tax returns and the returns of their related entities.

31. Upon reviewing the Home Concrete Return and the Election Document describing a positive basis adjustment, the Service selected the Taxpayers for audit commencing on January 25, 2006.

FIRST CLAIM FOR RELIEF

STATUTE OF LIMITATIONS

32. Plaintiffs/Petitioners incorporate paragraphs 1 through 31 as if fully set forth herein.

33. The adjustments set forth in the FPAA for the tax year ended December 31, 1999 are barred in their entirety by the three-year statute of limitations in Code §§ 6229 and 6501, which expired on April 17, 2003.

34. All of Home Concrete's gross receipts were disclosed on the Home Concrete Return, thus there has not been a substantial omission of gross income.

35. In the alternative, the six-year statute of limitations provided for in Code §§ 6229(c)(2) and 6501(e) is not applicable to Home Concrete or the Taxpayers, because any amount omitted from gross income (including any omitted amount attributable to the basis adjustment) was disclosed in the returns of Home Concrete and the Taxpayers, or in a statement attached to such returns, in a manner adequate to apprise the Commissioner of the nature and amount of such item(s).

36. The three-year period of limitations for assessment provided for in Code §§ 6229 and 6501 have expired and the six-year period of limitations for assessment is inapplicable. Therefore, no part of the adjust-

ments set forth in the FPAA would result in an increase to the Taxpayers' tax liability for any tax year currently open under the statute of limitations periods provided for in Code §§ 6229 or 6501, and all adjustments set forth in the FPAA are time-barred.

SECOND CLAIM FOR RELIEF

COMMISSIONER'S ERRORS

37. Plaintiffs/Petitioners incorporate paragraphs 1 through 36 as if fully set forth herein.

38. The Commissioner erred in making each and every adjustment set forth in the FPAA.

39. All items of income, loss, deduction and credit of Home Concrete for the tax year ended December 31, 1999 were properly determined and reported by the Taxpayers with reasonable care and good faith, and with reasonable and good faith reliance on the advice of professional tax advisors.

II. PRAYER FOR RELIEF

WHEREFORE, Plaintiffs/Petitioners respectfully pray this Court for:

(i) Judgment that adjustments, interest and penalties asserted by Defendant/Respondent are time-barred;

(ii) Judgment against Defendant/Respondent and declaration that the FPAA is invalid or alternatively to order Defendant/Respondent to reverse the adjustments set forth in the FPAA;

(iii) Return to Plaintiff/Petitioner Robert Pierce the $1,392,118.00 deposit plus interest; and

(iv) Such further relief, legal or equitable, to which Plaintiffs/Petitioners may be entitled.

This the 4th day of December, 2006.

WOMBLE CARLYLE SANDRIDGE & RICE
A Professional Limited Liability Company

By: /s/ ROBERT T. NUMBERS II
RICHARD T. RICE
(N.C. State Bar No. 9846)
ROBERT T. NUMBERS, II
(N.C. State Bar No. 34134)
One West Fourth Street
Winston-Salem, North Carolina 27101
(336) 721-3600
Attorneys for Plaintiffs/Petitioners

UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA

No. 7:06-CV-00181-FL

HOME CONCRETE & SUPPLY, LLC ET AL., PLAINTIFFS

v.

UNITED STATES OF AMERICA, DEFENDANT

[Filed: Feb. 26, 2007]

UNITED STATES' FIRST AMENDED ANSWER

In accordance with FED. R. CIV. P. 15(a), the United States provides the following first amended answer to the plaintiffs' complaint:

INTRODUCTION

1. Paragraph 1 does not require an answer.

PARTIES

2. Admits that Home Concrete & Supply, LLC was formed as a limited liability company under Delaware law. Denies that Home Concrete & Supply, LLC is treated as a partnership for federal tax purposes. Presently without sufficient knowledge or information to form a belief as to the truth of the remaining allegations in paragraph 2.

3. Admits that Robert L. Pierce is listed as the Tax Matters Partner on Home Concrete & Supply's 1999 Form 1065. Presently without sufficient knowledge or information to form a belief as to the truth of the remaining allegations in paragraph 3.

4. Admits that Stephen R. Chandler is listed as a partner on Home Concrete & Supply's 1999 Form 1065. Presently without sufficient knowledge or information to form a belief as to the truth of the remaining allegations in paragraph 4.

5. Admits that Home Oil and Coal Company, Inc. was formed as a corporation under North Carolina law. Admits that Home Oil and Coal Company, Inc. is listed as a partner on Home Concrete & Supply's 1999 Form 1065. Presently without sufficient knowledge or information to form a belief as to the truth of the remaining allegations in paragraph 5.

6. Paragraph 6 does not require an answer.

7. Admits the allegations in paragraph 7.

JURISDICTION AND VENUE

8. The United States incorporates its answers to paragraphs 1 through 7 as if fully set forth here.

9. Admits the allegations in paragraph 9.

10. Admits the allegations in paragraph 10.

11. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 11.

12. Admits the allegations in paragraph 12.

13. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 13.

ALLEGED FACTS

14. The United States incorporates its answers to paragraphs 1 through 13 as if fully set forth here.

15. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 15.

16. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 16.

17. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 17.

18. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 18.

19. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 19 and all of its subparts.

20. Denies the allegations in paragraph 20.

21. Presently without sufficient knowledge or information to form a belief as to the truth of the allegations in paragraph 21.

22. Admits that Home Concrete & Supply timely filed its 1999 Form 1065 on or prior to April 17, 2000. Admits that Home Concrete & Supply's 1999 Form 1065 included an attachment titled "ELECTION

TO ADJUST BASIS OF PARTNERSHIP PROPERTY." Admits that the attachment included a chart showing basis adjustments to various groups of assets. Admits that the IRS determined that the basis adjustments were invalid. Denies the remaining allegations in paragraph 22.

23. Admits the allegations in paragraph 23.

24. Admits that Home Oil filed its 1999 Form 1120S on or before April 17, 2000. Denies the remaining allegations in paragraph 24.

25. Admits that Robert and Susanne Pierce filed their joint 1999 Form 1040 on or before April 17, 2000. Denies the remaining allegations in paragraph 25.

26. Admits that Stephen and Rebecca Chandler filed their joint 1999 Form 1040 on or before April 17, 2000. Denies the remaining allegations in paragraph 25.

27. Denies the allegations in paragraph 27.

28. Denies the allegations in paragraph 28.

29. Denies the allegations in paragraph 29.

30. Admits the allegations in paragraph 30.

31. Admits that the IRS examined Home Concrete & Supply's 1999 Form 1065. Denies the remaining allegations in paragraph 31.

FIRST CLAIM FOR RELIEF

32. The United States incorporates its answers to paragraphs 1 through 31 as if fully set forth here.

33. Denies the allegations in paragraph 33.

34. Denies the allegations in paragraph 34.

35. Denies the allegations in paragraph 35.

36. Denies the allegations in paragraph 36.

SECOND CLAIM FOR RELIEF

37. The United States incorporates its answers to paragraphs 1 through 36 as if fully set forth here.

38. Denies the allegations in paragraph 38.

39. Denies the allegations in paragraph 39.

6-YEAR STATUTE OF LIMITATIONS DEFENSE

40. Although self-evident by its denial of paragraphs 33 through 36, the United States specifically pleads that the FPAA issued to the plaintiffs was timely under the six-year statute of limitations provided by 26 U.S.C. §§ 6501(e)(1)(A) and/or 6229(c)(2).

41. The amount of gross income omitted from the plaintiffs' 1999 tax returns exceeds the 25 percent threshold established by section 6501(e)(1)(A) and 6229(c)(2).

42. The plaintiffs' 1999 assessment limitations periods were suspended pursuant to 26 U.S.C. § 7609(e). Summonses with respect to the plaintiffs' 1999 tax liabilities were issued to Jenkens & Gilchrist on May 21, 2002 and June 19, 2003. Jenkens did not honor those summonses until sometime after May 16, 2004. *See* Pl. Comp. at ¶ 30.

Any allegation not explicitly admitted above is denied. The United States asks the Court to dismiss the plain-

tiffs' complaint with prejudice and grant the United States all relief to which it is justly entitled.

This 26th day of February 2007.

GEORGE E. B. HOLDING
UNITED STATES ATTORNEY

/s/ CHRISTOPHER R. EGAN
GROVER HARTT, III
Tex. Bar. No. 09174500
CHRISTOPHER R. EGAN
Tex. Bar. No. 24036516
Attorneys, Tax Division
Department of Justice
717 N. Harwood St., Suite 400
Dallas, Texas 75201
Phone: (214) 880-9732
Fax: (214) 880-9741

ATTORNEYS FOR THE UNITED STATES

CERTIFICATE OF SERVICE

I hereby certify that on February 26, 2007, I electronically filed the foregoing document with the Clerk of the court using the ECF system, which will send notification of such filing to the following:

Richard T. Rice
Robert T. Numbers, II
One West Fourth Street
Winstons-Salem, NC 27101

/s/ *Christopher R. Egan*
CHRISTOPHER R. EGAN

Jenkens & Gilchrist
A PROFESSIONAL CORPORATION
225 WEST WASHINGTON STREET
SUITE 2800
CHICAGO, ILLINOIS 60606-3418
(312) 425-3900
FACSIMILE (312) 425-3909
www.jenkens.com

January 31, 2000

CONFIDENTIAL
ATTORNEY-CLIENT PRIVILEGED

Mr. Stephen R. Chandler
[REDACTED]
Salisbury, North Carolina [REDACTED]

Dear Mr. Chandler:

You have requested us to review the United States federal income tax consequences of a number of transactions in which you have been involved and to provide our opinion regarding certain material United States federal income tax issues. Such transactions are described below under the heading "Facts."

In connection with this opinion, we have examined such matters of law, and such corporate and limited liability company records and such other agreements, certificates, instruments and documents, and we have made such other inquiries of officers, owners and representatives of the entities involved, as we have deemed necessary to render the opinions set forth herein. We have

without any investigation or independent confirmation relied upon and assumed the accuracy of the responses to such inquiries and such certificates, corporate and limited liability company records and other documents with respect to factual matters.

FACTS

In particular, our opinion is based upon the following facts:

1. On June 11, 1999, Home Oil & Coal Co., Inc. transferred substantially all of its business assets (the "Business Assets") to Home Concrete & Supply, LLC (the "Company"), a limited liability company, as a contribution to capital.

2. On May 13, 1999, you, through a Delaware limited liability company wholly owned by you, Goodnight Investments LLC (hereinafter referred to as "GILLC"), engaged in a transaction commonly referred to as a "short sale," in which you sold $1.387 million face value Treasury Notes maturing January 31, 2001 (the "Securities"), for $1,389,164.25 plus interest of $20,718.79, for total proceeds equal to $1,409,883.04.

3. On May 17, 1999, you transferred the proceeds from the sale of the Securities, together with the short Treasury Note position and $30,400.00 margin cash as a contribution to capital of the Company. You continued to maintain additional margin in your account to support any losses in the event the short securities position went down in value.

4. On May 18, 1999, the Company closed its short securities position by buying Treasury Notes in the market and "covering" its short position.

5. On June 14, 1999, you contributed a 0.3267% interest in the Company to Home Oil & Coal Co. Inc. ("HOCC INC.") as a contribution to its capital. The holdings of the Company on such date were cash and the Business Assets. The Company made, or intends to make, with respect to its 1999 taxable year, an election pursuant to section 754 of the Internal Revenue Code of 1986, as amended (the "Code").

OPINION

Based on the following discussion and analysis and subject to the qualifications, limitations and assumptions set forth herein, we are of the opinion that under current U.S. federal income tax law it is more likely than not that:

A. GILLC, as a single member limited liability company, should be disregarded for Federal income tax purposes.

B. The short sale of Treasury Notes should not be a taxable transaction.

C. The Partnership should be classified as a partnership for federal income tax purposes.

D. Your contributions of the cash and the short Treasury Notes position to the Company should not be taxable transactions.

E. The short Treasury Notes position should not be a liability within the meaning of Code section 752.

F. Your basis in your interest in the Company after the contribution of cash and the short securities position should be increased by the cash contrib-

uted, without adjustment for the short sale obligation.

G. The closing of the short sale position by the Company should not result in a deemed distribution to you for federal income tax purposes and the provisions of Code section 705(a)(2)(B) should not apply; consequently, no adjustment to your adjusted basis in your Company interest should be required as a result of the Company closing the short Treasury Notes position.

H. Your contribution of your interest in the Company to HOCC INC. should not be a taxable transaction.

I. Your basis in the stock of HOCC INC. should be increased by an amount equal to the adjusted basis of your interest in the Company as of the date of contribution.

J. HOCC INC.'s basis in the Company should be an amount equal to your basis in the contributed interest in the Company.

K. The effect of the Code section 754 election should be that the Company's basis in its property should be increased with respect to HOCC INC.

L. The step transaction and sham transaction doctrines should not apply.

M. Treasury Regulation section ("Treas. Reg. sec") 1.701-2 should not apply to the transactions described herein.

Each of the conclusions set forth above is supported by "substantial authority," and relevant tax positions

reported by you, the Company and HOCC INC. in accordance therewith are, as described, "more likely than not proper," as those terms are used in Code section 6662.

The opinions set forth above are subject to the following qualifications, limitations and exceptions:

No opinion is expressed about the tax treatment of the described transaction for purposes of any state or local income tax, or any tax other than the United States federal income tax.

Any misstatement of a material fact or omission of any fact that may be material or any change in any of the facts referred to may require a modification of all or a part of our opinions.

Our opinions are limited to the matters expressly set forth herein and no opinion may be implied or inferred beyond the matters so stated. The opinions expressed herein are based upon our interpretation of current law. The opinions expressed herein are not binding on the Internal Revenue Service ("IRS" or "Service") or the courts, and there can be no assurance that the IRS and the courts will not take a position contrary to the opinions expressed herein. We do not undertake to advise you of any changes in law which may occur after the date hereof. The Code, the regulations promulgated thereunder, and the administrative position of the IRS are subject to change either prospectively or retroactively. Such changes could render certain or all of the opinions expressed herein inapplicable.

For purposes of all of the above opinions, we are relying on the truth of the representations of you and/or members of the Company, or authorized officers of HOCC INC.

The opinions expressed herein are furnished by us solely for your benefit and for the benefit of the Company and HOCC INC. and they may not be relied upon or delivered to any person other than you, the Company and HOCC INC. and the successors or assigns of those persons without our express, prior written approval.

REPRESENTATIONS

You, authorized officers of HOCC INC. and/or members of the Company have represented the following:

a. You entered into the sale of the Treasury Notes for substantial nontax business reasons, including (i) to produce overall economic profits because of your belief that the short end of the U.S. Treasury interest yield curve would change; and (ii) your belief that the most direct way, with the most leverage, to realize gain from expected change in interest rates was the short sale of the Treasury Notes.

b. You contributed the short Treasury Notes position to the Company for substantial nontax business reasons.

c. The decision to close the short position in the Treasury Notes was based upon the belief that substantial interest rate changes in the near term were unlikely and that the market had already adjusted for the interest rate changes expected.

d. Your contribution of your interest in the Company to HOCC INC. was made for substantial nontax business reasons.

e. Neither you, GILLC, the Company, nor HOCC INC. were obligated to engage in any transaction to which our opinions herein relate upon the completion of any other of such transactions.

f. To the best of your knowledge, you have provided to us all the facts and circumstances necessary for us to form our opinion.

APPLICABLE LAW

Our analysis of the applicable United States federal income tax law with respect to the above stated facts and in support of each of the lettered opinions as set forth on pages 3 and 4 hereof is attached, with each attachment lettered to correspond to each such opinion.

Based on the foregoing and subject to the qualifications, limitations and assumptions set forth herein, we are of the opinion that the described tax consequences have substantial authority and that it is more likely than not that you will prevail if challenged by the IRS.

Very truly yours,

/s/ JENKINS & GILCHRIST
JENKENS & GILCHRIST

A. SINGLE MEMBER LLC DISREGARDED FOR FEDERAL INCOME TAX PURPOSES

General

The IRS issued revised regulations promulgated under Code section 7701 on December 17, 1996 (the "Classification Regulations"). T.D. 8697. In general, these regulations provide that, effective January 1, 1997, any domestic business entity which is not a corporation and which has a single owner will be disregarded as an entity separate from its owner unless the entity elects otherwise. Treas. Reg. §301.7701-3(b)(1)(ii).

Goodnight Investments LLC

GILLC was formed under a Certificate of Formation filed with the State of Delaware on April 15, 1999. GILLC is a domestic entity which is not a corporation and you own 100% of the membership interest in GILLC. Under the rules provided in the Treasury Regulations, GILLC should be disregarded as a separate entity. Neither you nor GILLC elected nor intend to elect to be classified as a partnership or as an association taxable as a corporation. Accordingly, it is more likely than not that the IRS should regard you as the owner of assets held in the name of GILLC.

B. TAX EFFECT OF MAKING A SHORT SALE

A "short sale" is a contractual obligation pursuant to which the seller is obligated to make delivery of a specified amount of specified property at some date in the future. The amount to be received by the seller is fixed on the date of the sale. If the property can be purchased at a lower price by the date of delivery, the seller will realize a gain; if the property increases in value and

must be purchased at a higher price, the seller will realize a loss. In a typical short sale transaction, the seller borrows the property which is the subject of the short sale and sells it on the open market. The seller, therefore, has possession of the proceeds from such sale, and an executory obligation to return the property to the lender, which generally must be secured by the sales proceeds.

The transaction is not completed for federal income tax purposes until such time as the sale is "closed," when delivery of property to "cover" the obligation arising from the property borrowing is made. Treas. Reg. sec. 1.1233-1(a)(1) states the rule as follows: "For income tax purposes a short sale is not deemed to be consummated until delivery of property to close the short sale."

The above described treatment is nearly as old as the U.S. income tax, which is evidenced by Solicitor's Opinion[1] 1179, 1 C.B. 60 (1919). In that Opinion, a short sale was held to remain an open transaction until the security sold short is repurchased for return to the lender and the transaction closed.

Accordingly, it is more likely than not that entering into the securities borrowing transactions and realizing cash proceeds from the sale of the borrowed securities, here, the January 31, 2001 Treasury Notes, should not be taxable events.

---

[1] A "Solicitor's Opinion" was the predecessor to the current General Counsel Memorandum.

C. CLASSIFICATION OF THE COMPANY AS A PARTNERSHIP FOR FEDERAL INCOME TAX PURPOSES

In determining the tax consequences of the transactions involving the Company, a threshold issue is its classification for federal tax purposes. Code section 7701(a)(2) defines the term "partnership" to include a syndicate, group, pool, joint venture, or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on, and which is not, within the meaning of the Code, a trust, estate or corporation. See also Code section 761(a). The term "partner" includes a member in such a syndicate, group, pool joint venture or organization. Code section 7701(a)(2). The classification of an entity as a partnership under state law is not determinative of its classification for federal tax purposes.

Under the Classification Regulations, effective January 1, 1997, any business entity which is not classified as a corporation for federal tax purposes, and which has two or more owners can choose to be classified as either a partnership or an association taxable as a corporation, and if no such election is made, will by default be classified as a partnership. Treas. Reg. sec. 301.7701-2, -3. Entities which are classified as corporations for federal tax purposes include (1) a business entity organized under a Federal or State statute, or under a statute of a federally recognized Indian tribe, if the statute describes or refers to the entity as incorporated or as a corporation, body corporate or body politic; (2) an entity which elects to be classified as an association; (3) a business entity organized under a State statute, if the statute describes or refers to the entity as a joint stock com-

pany or joint-stock association; (4) an insurance company; (5) a State-chartered business entity conducting banking activities; (6) a business entity wholly owned by a state or political subdivision thereof; (7) a business entity that is taxable as a corporation under a provision of the Code other than section 7701(a)(3); and (8) certain foreign entities, as more fully provided in the Treasury Regulations. Treas. Reg. sec. 301.7701-2(b).

Home Concrete & Supply, LLC

Home Concrete & Supply, LLC, a Delaware limited liability company, was formed under and governed by an Operating Agreement dated April 15, 1999 ("Operating Agreement"). Five (members) persons owned equity interests in the Company. Neither the Company nor any member has filed an election to treat the Company as an association taxable as a corporation. The Company did not constitute a corporation under any other provision of the Treasury Regulations. Accordingly, it is more likely than not that the IRS should regard the Company as a partnership rather than a corporation for tax purposes.

Potential IRS Arguments

There are three grounds on which the IRS conceivably could argue that the Company should not be treated as a partnership for federal tax purposes. First, the IRS might allege that the Company lacked a profit motive. To this end, the IRS perhaps would claim that the partners used the Company to serve tax purposes. Second, the IRS could allege that no true partnership existed. For reasons set forth below, you more likely than not will prevail if the IRS challenges the classification of the Company on either of these grounds. Finally,

the IRS might argue that the Company should be disregarded pursuant to the Subchapter K anti-abuse regulation. That regulation is analyzed separately in this opinion.

It is generally understood that to qualify as a partnership for tax purposes, the organization must have a profit objective. Hence, a venture formed to pursue a hobby or artistic interest, instead of economic profits, has been held not to constitute a partnership for income tax purposes. *Ewing v Commissioner*, 20 T.C. 216 (1953), affd. 213 F.2d 438 (2d Cir. 1954). However, the Tax Court has treated a tax shelter limited partnership as a partnership for tax purposes despite its determination that the entity lacked a profit motive. *Brannen v. Commissioner*, 78 T.C. 471, 512n. 16 (1982), affd. 722 F.2d 695 (11th Cir. 1984). See also *National Commodity & Barter Association v. United States*, 843 F.Supp. 655 (D. Colo 1993) (membership organization that carried on financial operations and tax protester activities lacked profit motive but was classified as a partnership). In addition, the IRS has on at least one occasion indicated that the absence of a joint profit motive does not prevent an arrangement from being a partnership for tax purposes. In PLR 7903084, the IRS classified an arrangement between co-owners of environmental protection equipment as a partnership, even though the arrangement lacked a joint profit motive. In reaching this conclusion, the IRS stated that the classification principles set forth in Treas. Reg. sec. 301.7701-2 "were developed without reference to, and do not definitely cover, unincorporated organizations (other than trusts) that are engaged in not-for-profit activities." The IRS has also ruled that an unincorporated organization with no profit

objective may be classified as a partnership. PLR 9108025 (November 26, 1990).

Assuming that a profit objective is required of entities classified as partnerships for tax purposes, it has been represented that the Company possessed that objective. Further, the presence of a tax motive in the formation or use of a partnership historically has never prevented a partnership from classification as such for tax purposes. *See e.g., Commissioner v. Culbertson*, 337 U.S. 733 (1949); *Slifka v. Commissioner*, 182 F.2d 345 (2d Cir. 1950).

With respect to whether a partnership actually exists, in the case of *ASA Investerings Partnership v. Commissioner*, T.C. Memo. 1998-305, the Tax Court held that no partnership existed for federal income tax purposes between AlliedSignal Inc. and a foreign commercial bank. In that case, the partnership, which was primarily capitalized with contributions from such foreign partner, invested in high-grade, floating-rate private placement notes ("PPNs"). The PPNs were subsequently sold in an installment sale in which the consideration was cash and LIBOR-indexed installment notes. Due to the structure of the sale, a large portion of the PPNs' tax basis was allocated to the LIBOR notes. Additional financial instruments were purchased by the partnership, and later AlliedSignal purchased most of the foreign partner's interest in the partnership. The LIBOR notes were distributed to AlliedSignal, which subsequently sold such notes, generating a large capital loss. While a partnership agreement had been entered into by the parties, other agreements regarding the economics of the series of transactions were also in place. The result of such other agreements was that the foreign partner

was to get a certain specified return on its contribution to the partnership. The Court held that to form a valid partnership the parties must have intended to join together in the present conduct of an enterprise, and found, as a factual matter, that the purported partners of ASA had divergent business goals. The Court found that, considering all of the facts and circumstances, the foreign partner was, in reality, a creditor to AlliedSignal, rather than its partner.

In the case of the Company, each of the members intended to join together in the common purpose of investing in short U.S. Treasury obligations and other financial instruments and investments and sharing the losses and profits therefrom. No member's share was guaranteed or limited. Accordingly, it is more likely than not that the analysis employed by the Court in *ASA* should be inapplicable and the partnership should be respected.

D. YOUR CONTRIBUTIONS TO THE COMPANY WERE NOT TAXABLE TRANSACTIONS

Code section 721(a) provides the general rule that:

> "No gain or loss shall be recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership."

There are certain exceptions to the above stated general rule, none of which are applicable here. For example, a transfer to a partnership which would be treated as an investment company under the principles of Code section 351(e)(1) might require the recognition of gain or loss. A transfer of property will be considered to be a transfer to an investment company if (1) the transfer

results, directly or indirectly, in diversification of the transferors' interests; and (2) the transferee is either (a) a regulated investment company (RIC), (b) a real estate investment trust (REIT), or (c) a company more than 80 percent of the value of whose assets (excluding cash) are held for investment and are readily marketable stocks or securities or interests in RICs or REITs. Treas. Reg. sec. 1.351-1(c). Here, the assets transferred to the Company were the Business Assets and cash. The short securities position, while a type of investment, represented an economic obligation. Since the Company is not a RIC or a REIT and has less than 80% of its value represented by investments in marketable securities, it is more likely than not that your contribution to the Company was not a taxable transaction.

Other instances in which income or gain might be required to be recognized upon the transfer to a partnership include when debt relief exceeds the basis of property transferred under the principles of Code section 752,[2] or if the contribution were a disguised sale of property to the entity under the principles of Code section 707. In this case, such exceptions are inapplicable and the general rule of nonrecognition of gain more likely than not should apply to your contributions of the cash and the short Treasury Notes position to the Company.

---

[2] As discussed in Section E, below, the short sale obligation transferred to the Company should not constitute a "liability" for purposes of Code section 752; additionally, such contingent obligations are generally not taken into account for federal income tax purposes in tax-free transactions, such as partnership formations under Code section 721, in accordance with a "step into the shoes" approach. *See, e.g.*, Keyes and Mandarino, "Dealing With Contingent Stock and Contingent Liabilities in Tax-Free Transactions," 52 N.Y.U. 24 (1994).

E. TREATMENT UNDER CODE SECTION 752 OF BORROWING OF TREASURY NOTES TO EFFECT A SHORT SALE

For the following reasons, it is more likely than not that the short sale obligations should not be treated as liabilities of the Company for purposes of Code section 752.[4]

Short Sales, Generally

A useful explanation of a completed short sale and the series of distinct transactions comprising it was presented by the Supreme Court in *Provost v. United States*, 269 U.S. 443 (1926); 1 U.S.T.C. ¶ 153. The issue in that case was whether the borrowing and the return of stock were taxable events subject to the stamp tax. Before concluding that they each were, the Supreme Court explained,

> "The loan of stock is usually, though not necessarily, incidental to a 'short sale.' As the phrase indicates, a short sale is a contract for the sale of shares which the seller does not own or the certificates for which are not within his control so as to be available for delivery at the time when, under the rules of the Exchange, delivery must be made.
>
> * * * * *
>
> It will be observed that the completed short sale transaction usually involves four separate steps in each of which there is either a sale or a complete transfer of all the legal elements of ownership. These

---

[4] *See, also*, Alice Welt Cunningham, "Short-Sale Obligations and Basis in Partnership Interests," 72 Tax Notes 1663-74 (Sept. 23, 1996).

> are (1) the sale of the stock by the person effecting the short sale, followed by the transfer and delivery of the certificates for the borrowed stock to the purchaser's broker; (2) the transfer of the shares from the lender to the borrower, who uses them for delivery on the customer's short sale; (3) the purchase by the borrowing broker of the stock required to repay the loan; (4) the transfer and delivery by the borrower to the lender of the certificates for the purchased shares to replace the shares borrowed. Each transfer may be accompanied by a physical delivery of certificates of the stock transferred; but the intermediate deliveries in (2) and (3) are usually eliminated by use of the Stock Exchange Clearing House."

269 U.S. at 450-453.

The taxpayers in *Provost* urged the Court to treat the borrowing of stock as in substance a mere pledge of stock, which would not be subject to the tax. The Court disagreed, emphasizing that the borrowing must be recognized for what it is—a separate, substantive transfer bearing distinct legal characteristics.

Code Section 752 and Related Authorities

Code section 752(a) treats any increase in a partner's share of liabilities of a partnership as a deemed contribution of money by such partner to the partnership, thus increasing basis. Code section 752, however, which governs the "treatment of partnership liabilities," does not define "liabilities." Resolution of this issue turns on the substantial case law and the definition provided in former Temp. Treas. Reg. sec. 1:752-1. We reach our conclusion noted above by virtue of the contingent nature of borrowings of securities in connection with a short sale,

the analogous obligations which have been held not to constitute liabilities under Code section 752, the relationship between partnership liabilities and debt under Temp. Treas. Reg. sec. 1.752-1T (as originally proposed), and the absence of any basis created by the borrowing.

The courts have consistently held that obligations which are contingent or speculative are not liabilities for purposes of Code section 752, a principle which the IRS has consistently followed. See *Long v. Commissioner*, 660 F.2d 416 (10th Cir. 1981), affg. 71 T.C. 1 (1979); *Brountas v. Commissioner*, 692 F.2d 152 (1st Cir. 1982). This line of authority is based on the theory that underlies authorities holding that contingent or speculative obligations cannot give rise to basis. See *Denver & Rio Grande Western Railroad Co. v. United States*, 505 F.2d 1266 (Ct. Cl. 1974); *Lemery v. Commissioner*, 52 T.C. 367 (1969), aff'd. 451 F.2d 173 (9th Cir. 1971).

In *Long*, the Tenth Circuit addressed whether certain contested claims against a partnership were liabilities under Code section 752. In holding that the obligations were not, the court stated,

> "The Tax Court held that because the lawsuit claims against the partnership were indefinite and contingent liabilities, they should not be recognized for basis adjustment purposes *until the exact amounts of the liabilities were established.* After the parties settled those suits, the Tax Court treated the settlement totals plus attorneys' fees incurred as partnership liabilities and permitted adjustment of the estate's basis in the partnership interest to the extent of its 25% interest. *See* 1 W. McKee, W. Nelson & R. Whit-

mire, Federal Taxation of Partnerships and Partners ¶ 7.01[2] (1977). We agree with this approach and holding. [Emphasis added.]"

Brountas involved an oil and gas drilling partnership investment partially paid with nonrecourse obligations that were to be satisfied only out of oil production payments. The First Circuit (Judge Breyer) characterized the obligation as highly contingent and speculative and seeming "less like the repayment obligation that typically accompanies a recourse loan than like a device for sharing business risks—the risks that accompany oil explorations." 692 F.2d 158. Hence, the court held, *inter alia*, that the obligations were not partnership liabilities for purposes of Code section 752.

In determining whether an obligation is contingent, the analysis generally stops abruptly at the terms of the obligation if those terms objectively impose a contingency. See *Denver & Rio Grande Western Railroad Co. v. United States*; 505 F.2d 1266 (Ct. Cl. 1974); *Lemery v. Commissioner*, 52 T.C. 367 (1969), affd. 451 F.2d 173 (9th Cir. 1971); PLR 7704269550A("When the documents, by their terms, create only contingent obligations, Courts ordinarily will not look beyond the documents to determine the intent of the parties.")

In *Denver & Rio Grande Western Railroad Co.*, 505 F.2d at 1269-70, the court refused to allow the railroad taxpayer to include in its basis advances by a customer (used to build a "spur line") which were repayable only out of proceeds from shipping above a certain annual tonnage for 10 years. The taxpayer argued that the obligation was not contingent because in light of the underlying facts and circumstances it could be predicted with

"reasonable certainty" that the advances would be repaid in full. The court rejected the argument, stating it does not matter what the parties' subjective intentions were. Absent a binding obligation to repay all of the advances at the time the subject deductions were taken, the court considered it "impossible" to value the obligation assumed.

In *Lemery*, 52 T.C. at 377-78, the court held that an obligation to pay part of the purchase price of a business out of "net profit" was too contingent to be included in the purchaser's basis. The petitioners were unsuccessful in arguing that, although the amount was contingent, the liability itself was absolute.

By its terms, the borrowing of a security to effect a short sale is both contingent and speculative. There is no certainty as to the amount of the obligation until the short sale is completed. If perchance the security becomes worthless while borrowed, the obligation is similarly worthless. In fact, borrowings of securities to effect short sales present a more compelling case of a contingent obligation than these in the cases discussed above, because the obligor's *desired, if not expected, result* is for the value of the obligation to decline.

In a directly analogous case involving this rule, *LaRue v. Commissioner*, 90 T.C. 465 (1988), the court held that liabilities attributable to an accrual basis partnership's deductible expenses must meet the "all events" test of Code section 461 (described below) before they would be considered "liabilities" for inclusion in the basis of a partner's partnership interest. In *LaRue*, LaRue was a general partner of Goodbody and Co. ("Goodbody"), a large stock brokerage firm. Due to the

inability of recordkeeping technology at the time to keep up with trading volume, Goodbody incurred large, unanticipated "back office" liabilities. These back office liabilities were created by the following types of transactions:

(1) Fails to Receive—Securities which the broker should have purchased at a stated price were not purchased. Gain or loss would be incurred on these transactions measured by the difference between the customer's contract price and what the broker had to pay to obtain the securities. These transactions were the functional equivalent of short sale transactions.

(2) Fails to Deliver—Securities which the broker thought were sold to another broker but for which no "comparison" for proof could be provided. These securities then had to be sold and the gain or loss incurred was measured by the difference between the original sales price and the actual proceeds received.

(3) Securities Differences—These represented differences between the securities the broker's records stated it should be holding for its own or other's accounts and the securities actually "in the box." These resulted mainly from incorrect deliveries, receipts, or thefts. Gain or loss was measured by the value of excess securities or their replacement cost.

(4) Dividend Errors—The broker was responsible to its customers for dividends and interest on securities which it held as nominee for its customers, that is securities held in "street name." If the broker failed to receive a dividend or interest payment when due it was still liable to its customer for such amount.

Due to the large losses generated by these back office problems and the withdrawal of capital by subordinated lenders, Goodbody was in violation of the New York Stock Exchange minimum capital requirements. At the same time, another brokerage firm, Merrill Lynch, agreed to acquire Goodbody. The acquisition transaction raised the issue as to whether LaRue, and the other Goodbody partners, could include the back office liabilities in the bases of their partnership interests.

The *LaRue* court held that the Goodbody partners could *not* include these back office liabilities in their bases because the "all events" test had not been met. The court said:

> "Because an accrual-basis partnership uses the 'all-events' test to determine when an expense is deductible, we think that test may be properly used to determine when the corresponding liability is includable in basis."

The all-events test is met with respect to any item if all events have occurred which determine the fact of the liability and the amount of the liability can be determined with reasonable accuracy. Treas. Reg. sec. 1.461-1(a). The court stated that while Goodbody had a liability to its customers for their back office failures, the amount of these liabilities were not determinable with reasonable accuracy until any missing securities were purchased or excess securities were sold at the market price. The *LaRue* holding has not been overturned.

In the present case, the Company's obligation to return the Treasury Notes borrowed to effect the short sale closely parallels the obligations of Goodbody in *LaRue*. The Company clearly had an obligation to re-

turn Treasury Notes to the lender. However, the amount of that liability was not determinable with reasonable accuracy until the Company purchased those Treasury Notes on the open market. Thus, the all events test was not met because the amount of the Company's liability could not be reasonably determined, and it is more likely than not that the obligation with respect to the short sale should not be considered a liability under Code section 752.

That an obligation to return securities borrowed to effect a short sale is not a liability under Code section 752 is also theoretically consistent with the provisions of Code section 1233, which treats a short sale as an open transaction.[4] *See* Treas. Reg. sec. 1.1233-1(a)(1). The reason for holding the short sale transaction open until the short sale is covered is that, until such time, the borrower's tax basis in the underlying securities is unknown. *See* McCawley, 184-4th T.M. *Transactions in Stock, Securities and Other Financial Instruments* at A-19. This demonstrates that the borrowing of securities under a short sale does not create basis. If the short seller did receive a tax basis in the borrowed securities (which is not the case), it would not be necessary to keep the short sale open until it is covered.

---

[4] However, the IRS issued Field Service Advice 199913016 (December 23, 1998), which provides that it is the position of the IRS that the "open transaction" principle applies to gain or loss recognition timing for tax purposes, not to when a "short sale obligation's value" is included in the basis of partnership assets. It should be noted that in the case at hand, the Company is not including the short sale obligation's value in the basis of its assets, rather the Company is including the cash *proceeds* of the short sale in the basis of assets, pursuant to the rules provided in Subchapter K. This FSA seems to have been issued in connection with Rev. Rul. 95-26, discussed more fully below.

Congress could have chosen to give the borrower of securities in a short sale an immediate basis in such securities equal to their fair market value on the borrowing date, but Congress did not. Instead, Congress chose to treat the short sale liability as an open, contingent liability, which is closed at the time the short sale is covered.

The non-basis creating character of short sales as a performance obligation and not a monetary obligation was initially espoused in Revenue Ruling 57-29, 1957-1 C.B. 519. In that ruling, the IRS held that a seller of "when-issued securities" (the economic equivalent of a short sale)[5] does not receive a basis in his contractual obligation to deliver securities in kind to the buyer. As stated in the ruling:

> "In computing the cost basis of assets for any purpose, the IRS does not recognize an obligation of a taxpayer reflected in an executory contract prior to the performance of the contract."

Accordingly, contingent, open transactions, such as those created by securities borrowings incident to a short sale, should not give rise to basis under Code section 752.

The conclusion that borrowings of securities to effect a short sale are not partnership liabilities for tax purposes should be mandated for borrowings governed by former Temp. Treas. Reg. sec. 1.752-1T(g)(T.D. 8237, 53 F.R. 53,140, Dec. 30, 1988).[6] That regulation, which was

---

[5] Cf. Code section 1233(e)(2).

[6] On July 31, 1991, Treasury issued proposed regulations (the "Proposed Regulations") designed to "simplify the Temporary Regulations."

effective from December 29, 1988, through December 29, 1991, defined partnership liabilities as follows:

> "(g) **Liability defined.** Except as otherwise provided in the regulations under Section 752,[7] an obligation is a liability of the obligor for purposes of Section 752 and the regulations thereunder to the extent, *but only to the extent,* that incurring or holding such obligations gives rise to—
>
> (1) The creation of, or an increase in, the basis of any property owned by the obligor (including cash attributable to borrowings);
>
> (2) A deduction that is taken into account in computing the taxable income of the obligor; or
>
> (3) An expenditure that is not deductible in computing the obligor's taxable income and is not properly chargeable to capital.
>
> See examples (2) and (3)(ii) of paragraph (k) of this section. [Emphasis added.]"

(Preamble to PS-49-91 (Federal Register, July 31, 1991)). The Proposed Regulations, which are generally effective after December 28, 1991, delete entirely the definition of "liability" for purposes of Code section 752. The preamble to the Proposed Regulations does not reveal any substantive reason for this deletion, other than the streamlining of the Temporary Regulations. This appears to be confirmed by the IRS's failure to revoke Rev. Rul. 88-77 which contains a "liability" definition identical to that contained in theTemporary Regulations.

[7] "Notwithstanding the 'except as otherwise provided' proviso at the beginning of this definition, there appear to be no exceptions under which an obligation that satisfies any of the enumerated criteria is not a liability, or under which an obligation that does not satisfy any of the criteria is a liability." McKee, Nelson and Whitmire, *Federal Taxation of Partnerships and Partners*, ¶ 7.01[1] at n. 3. (2d ed. 1990).

Paragraph (k) of the regulation addressed the definition of partnership liability as follows:

> "**(k) Examples.** The following examples illustrate the application of the rules of this section. Except as otherwise provided, these examples assume that (1) the partnerships discussed therein are formed under state laws corresponding to the Uniform Partnership Act or the Revised Uniform Limited Partnership Act, whichever is appropriate, (2) partnership indebtedness constitutes debt for federal income tax purposes, and (3) any debt instrument given in consideration for the sale or exchange of property bears adequate stated interest (within the meaning of section 1274(c)).
>
> * * * * *
>
> Example (2). (i) C and D are partners in a general partnership that uses the cash method of accounting. At the close of its taxable year, the partnership has accrued interest expense of $1,000 and accounts payable of $500 for services performed on behalf of the partnership.
>
> (ii) Under its method of accounting, the partnership's accrued interest expense and accounts payable are not deductible until paid. Also, the partnership obligations represented by those items have not created or increased the basis of any partnership property or given rise to a nondeductible expenditure of the partnership that is not properly chargeable to capital account. As provided by paragraph (g) of this section, *an obligation that constitutes a debt for federal income tax purposes is a liability of the obligor only to the extent that*

incurring or holding such obligation gives rise to (1) the creation of, or an increase in, the basis of any property owned by the obligor, (2) a deduction that is taken into account in computing the taxable income of the obligor, or (3) an expenditure that is not deductible incomputitlg the obligor's taxable income and is not properly chargeable to capital. Therefore, the partnership obligations for accrued but unpaid interest expense and accounts payable are not partnership liabilities for purposes of section 752.

Example (3). (i) E and F form a general partnership with cash contributions of $20,000 each. The partnership agreement provides that E and F will share all partnership profits and losses equally. The partnership purchases depreciable personal property for $40,000 in cash and a recourse purchase money note for $60,000.

(ii) The indebtedness represented by the purchase money note is a partnership liability because incurring that obligation creates an additional $60,000 of basis in the partnership's depreciable personal property. See paragraph (g) of this section. [Emphasis added.]"

While the above language of the temporary regulations was not part of the regulations when they were finalized in December, 1991 (see footnote 5, above), it nevertheless is indicative of the Treasury's position. The language of subsection (k) set forth above indicates that a partnership obligation governed by Temp. Treas. Reg. sec. 1.752-1T must first be debt for federal tax purposes to qualify as a partnership liability under Code

section 752. See *Chevron Corporation v. Commissioner*, 104 T.C. No. 35 (June 27, 1995) (regarding effect of examples under a regulation). It is well established that borrowings of stock for short sale purposes do not constitute debt for federal tax purposes. *Deputy v. duPont*, 308 U.S. 488 (1940); Rev. Rul. 95-8, 1995-4 IRB 29.

As the Supreme Court in *Deputy v. duPont* correctly analyzed in terms of a short sale of stock, "although an indebtedness is an obligation, an obligation is not necessarily an 'indebtedness'." In that case, the taxpayer, Pierre duPont, borrowed stock of E.I. duPont de Nemours and Company ("duPont") under an agreement whereby he agreed to return the stock loaned in kind within ten years and in the interim to pay to the lender all dividends declared and paid on the shares so loaned. The taxpayer then sold the borrowed shares to certain executives of duPont, for cash which such executives borrowed from duPont. It was thought desirable that these executives have a financial interest in duPont, but there were alleged legal prohibitions on the corporation itself selling the stock to them. When the ten-year term of the loan was about to expire, the taxpayer arranged for a new loan of securities from a different lender, in order to satisfy his obligation to the first lender. The second loan of duPont stock was similar to the first, in that it had a ten-year term, the obligation was to return the stock loaned in kind, and in the interim pay an amount equivalent to all dividends declared and paid on the borrowed shares, plus an amount equal to the lender's tax liability arisingby reason of the agreement. The IRS disallowed the deduction of the amounts paid to the second lender on the grounds that the payment was not an ordinary and necessary business expense of the tax-

payer, nor was it deductible interest. The disallowance was reversed on appeal, but upheld by the Supreme Court. On the first point, the Supreme Court held against the taxpayer, finding that, while the expenditures related to offering incentives to duPont's management may have been ordinary and necessary to duPont's business, they were not ordinary and necessary business expenditures of the taxpayer. On the second point, the Supreme Court also held against the taxpayer, finding that the ·payments relating to the security loan did not constitute interest, because the obligation to return the duPont shares was not an "indebtedness," and the amounts paid did not constitute "interest," which was defined as "compensation for the use or forbearance of money."

An identical concept to that provided in Temp. Treas. Reg. Sec. 1.752-1T(g) can be found in Revenue Ruling 88-77, 1988-2 C.B. 128, in which the IRS stated:

> "For purposes of Section 752 of the Code, the terms 'liabilities of a partnership' and 'partnership liabilities' include an obligation *only if and to the extent that* incurring the liability creates or increases the basis to the partnership of any of the partnership's assets (including cash attributable to borrowings), gives rise to an immediate deduction to the partnership, or, under Section 705(a)(2)(B), currently decreases a partner's basis in the partner's partnership interest. The preceding sentence uses the term 'assets' to include capitalized items that are properly allocable to future periods, such as organizational expenses and construction period expenses. [Emphasis added.]"

In accordance with this definition, Revenue Ruling 88-77 holds that a cash basis partnership's accounts payable for interest expense and services did not increase the tax basis of partnership interests under Code section 752.

Thus, a liability for Code section 752 purposes does not exist and no Code section 752 adjustment is appropriate in connection with a partnership obligation that does not increase the basis of partnership assets or generate either a deduction or a nondeductible, noncapital expenditure. Because a short sale does not create basis in the borrowed security, as noted, and does not generate either a deduction or a nondeductible, noncapital expenditure, the borrowing of the security used to effect the short sale should not constitute a liability under Code section 752.

The tax basis in the cash received when the borrowed securities are sold in the marketplace has no correlation with the obligation underlying the short sale, and should not cause a short sale to be characterized as a Code section 752 liability. The obligation is to return the physical securities in kind, while the cash represents the proceeds of sale. This is the case even though the partnership's receipt of cash as a contribution will cause a disparity between the "inside basis" of the partnership's assets, and the "outside basis" of partnership interests upon the closing of the short sale.

For example, in Revenue Ruling 73-301, 1973-2 C.B. 216, a partnership received cash progress payments on a construction contract reported under the completed contract method. The partnership distributed the cash to its partners. The issue was whether the partnership's

obligation under the contract caused the advance payments to constitute Code section 752 liabilities. If so, the cash distributions to the partners would not have exceeded the basis of the partners' interests. The IRS refused to accord Code section 752 liability treatment to the construction contract, stating:

> "The progress payments . . . received by the partnership and reflected as 'deferred income' on the books of the partnership . . . represent amounts received on account of services performed on the contract not yet reported as gross income. This amount together with the right of the partnership to an additional payment . . . for work performed constitute 'unrealized receivables' within the meaning of Section 751(c) of the Code, and the progress payments are not a 'liability' as referred to in Section 752 which increases the adjusted basis of the partnership interests of the partners. The income or loss from performance of the contract will affect the basis of the partnership interest in the partners, as provided in Section 705(a), when such income or loss is recognized for Federal income tax purposes.
>
> Accordingly, no increase in the adjusted basis of the partnership interests . . . is made as a result of the receipt by the partnership of the advance payments within the meaning of Section752(a) of the Code."

Therefore, the IRS disallowed a Code section 752 basis step- up, despite the resulting disparity between the inside basis of the partnership's assets and the outside basis of the partnership interests. A partnership which sells securities short is similar to the partnership that received advance payments in Rev. Rul. 73-301. Both

partnerships receive cash payments from a third party and both possess executory contractual obligations which did not directly give rise to basis at the partnership level when the obligation was incurred. Both contractual obligations are uncertain in amount in that the partnerships cannot precisely calculate the cost of fulfilling their obligations. Both partnerships are reporting their taxable income under specialized methods of accounting which permit deferral of taxable income until completion of performance under an executory contract: the completed contract method in the case of the Rev. Rul. 73-701 partnership and the short sale regulations in the case of a short selling partnership. Accordingly, like the partnership in Rev. Rul. 73-301, it is more likely than not that the Company received no Code section 752 basis from its obligation associated with the short sale.

Similarly, in *George Helmer v. Commissioner*, 34 TCM 727 (1975), the Tax Court held that a partnership's receipt of money pursuant to an option agreement did not create a partnership liability under Code section 752. In that case, a partnership owned certain real property on which it granted a corporation a purchase option. In consideration for the option, the corporation paid cash to the partnership. The partnership distributed the cash to its partners. The IRS argued that the option agreement did not create a partnership liability under Code section 752 and, thus, the distribution of the option money caused the partners to recognize gain under Code section 731 (i.e., the distribution of the option money exceeded the partners' tax bases in their partnership interests). The partners argued that the receipt of the option money created a short option partnership

liability under Code section 752 which increased the adjusted basis of their partnership interests.

The Tax Court held for the IRS, even though a disparity between partnership inside and outside basis resulted. The Tax Court stated:

> "We are faced with a unique situation. Helmer Brothers received payments pursuant to the option agreement when there was no forfeiture of any of the option payments, the option had not been terminated, nor had any portion of the option been exercised by the optionee. Respondent, in his brief, conceded that the income from the option payments was deferrable by the partnership until characterized as ordinary income (because of the default by the optionee) or capital gains (because of an exercise of the option by the optionee).
>
> * * * * * * *
>
> The moneys received under the option agreement were free of restrictions except that upon exercise of the option such amounts would be applied against the purchase price. Thus, the restriction only affected the character of the gain in the partnership's hands. It is this lack of ability to determine character of income (not any liability to repay or to perform) that causes the deferral of the recognition of the income by the partnership until the option is either exercised or lapsed."

From the standpoint of the option grantor, the liability created under an option is equivalent to the obligation of a short seller, except that the option is more speculative because it may expire "out of the money."

For example, consider the case of Smith who sells a call option to Jones, permitting Jones to purchase Apple stock at $100 from Smith. If the call option settles "in the money" at the expiration date, Smith will be required to deliver Apple stock to Jones in the same manner that a short seller would be required to deliver Apple stock to a brokerage house. Because of the similarity between an option and a short sale obligation, the *Helmer* case offers further justification for the conclusion that a short sale obligation is not a liability within the meaning of Code section 752.

Furthermore, it would be entirely inconsistent to create outside Code section 752 basis in the case of a short sale, yet not create outside basis for the premium received from an option sale such as that considered in *Helmer*. Consider, for example, a partnership which sells a "deep-in-the-money"call option on a Treasury note. Assume the partnership sells for $55 a call option with a $45 strike price on Treasury notes trading at $100. Under *Helmer*, the $55 option premium would not give rise to outside section 752 basis. This is the case even though the option is so deep-in-the-money that the partnership is effectively short the underlying Treasury notes. Similarly, no outside Code section 752 basis should be recognized by a partnership which receives $100 proceeds for merely selling Treasury notes short, as opposed to selling deep-in-the-money calls. Indeed, not following the *Helmer* decision in determining the outside basis for short sellers would create inconsistent tax results for taxpayers in economically equivalent positions.

Alternatively, consider a partnership which sells an at-the-money Treasury note call option for $10, when

Treasury notes are trading at $100. The partnership immediately invests the $10 in an at-the-money put option on Treasury notes. The resulting position is commonly referred to as a "synthetic short position." This is because the partnership's position is the economic equivalent of being short Treasury notes. (That is, the partnership has unlimited exposure if Treasury notes rise in value, but the partnership will earn, at most, $100 if Treasury notes fall to zero in value.) Under the *Helmer* decision, no liability exists under Code section 752 for the $10 option premium received by the partnership from the sale of the call option.

If *Helmer* were not similarly applied to a partnership that sells short Treasury notes for $100 (as opposed to creating a synthetic short sale), materially different tax positions would be accorded to identically situated taxpayers. In the first case, the partnership interests would have a basis of zero (*Helmer*); in the latter case, the partnership interests would have a basis of $100.

Here, the borrowings of Treasury Notes were analogous to the contractual obligations of the partnership in *Helmer*, since no income was recognized upon the short sale, the Company had no duty to return any cash to the buyer of those notes, and had at most a contingent obligation to use the proceeds to satisfy the contractual obligation to the lender of those notes. Again, the Company's case should be more compelling because, as discussed below, the cash received was attributable to the *sale* of the notes—not the obligation to return them.

A case involving the issue of whether a short sale of securities constitutes a liability for purposes of Code section 752 was filed with the Tax Court in November

1996 and is currently pending, *Salina Partnership L.P. v. Commissioner*, Docket No. 25084-96. In such case, the Petitioner challenged a determination that it had overstated its 1991 capital gains by failing to include a short sale position as a liability for purposes of determining the tax basis used in computing the gain. The case was tried December 6, 1999. A post-trial briefing schedule was set by the court. The last of the parties' briefs is scheduled to be filed in April 2000. It is unknown at this time when or how the Tax Court will rule.

Revenue Ruling 95-26

On March 9, 1995, the IRS released Revenue Ruling 95-26, 1995-1 C.B. 798, relating to the treatment of partnership liabilities. In that ruling the IRS concluded with remarkable brevity that a short sale of securities created a partnership liability under Code section 752. The IRS did not engage in any extensive (or even simplistic) analysis, and stated as its sole rationale that because the short sale creates an obligation on the part of the seller to return the borrowed securities, and the cash received in the short sale is an asset, the partnership's assets have increased in basis and therefore the short sale creates a liability. Curiously, the IRS cited *Deputy v. duPont* for this proposition.

The holding of *Deputy v. duPont* was cited by the IRS as the only relevant authority in Rev. Rul. 95-8, 1995-4 IRB 29, for the proposition that a short sale created an obligation, not an indebtedness. It is interesting to note that Rev. Rul. 95-8 was issued less than ten weeks before the issuance of Rev. Rul. 95-26. In Rev. Rul. 95-8 the IRS held that income attributed to a short sale transaction did not constitute unrelated debt-financed

income to a tax-exempt organization. Similarly, in the instant example, an obligation, and not an indebtedness (and, contrary to the IRS's most recent view, not a liability) has been incurred when a taxpayer borrows a security and *does not* then sell such security.

In addition to failing to distinguish the plethora of contrary preexisting authorities previously discussed, the IRS has also failed to analyze correctly the source of the basis in the cash referred to in the ruling. As the authorities set forth above indicate, it is clear that the taxpayer does not yet have a tax basis in the security, such tax basis will only arise if and when the taxpayer purchases a security that is redelivered to the lender in satisfaction of its obligation. If the taxpayer redelivers the same security, thus extinguishing the obligation, there is no necessity to determine tax basis, since no sale or exchange has occurred.

A short sale is essentially a multi-part transaction. See *Provost v. Commissioner*, 269 U.S. 443 (1926). First, the short seller borrows the securities in kind from a lender of the securities. The short seller at this point is possessed of a security, which it has borrowed, and has incurred an obligation to return that security in kind. The second transaction occurs when a taxpayer sells the borrowed security in the open market and realizes cash proceeds therefrom. It is thus obvious that the borrowing of the security—transaction 1—does not relate to the cash proceeds of the sale—transaction 2. The taxpayer has a basis in such cash proceeds because they are an "amount realized"on sale under Code section 1001(a), not because an obligation to repay in kind has been created.

The obligation in the short sale transaction ultimately will relate to the adjusted basis of the property for determining gain or loss under Code section 1011. The obligation will be satisfied by the purchase of a security which represents the *cost* of that security under Code section 1012. This amount constitutes a cost *offset* to the *cash amount realized* as proceeds of sale, resulting in gain or loss on the transaction.

By fixing the amount of the liability at the short sale price, Rev. Rul. 95-26 arguably creates gain or loss characterization distortions. For example, assume the security becomes worthless after the short sale. Would the gain be "cancellation of indebtedness" (ordinary) income? Also, assume the security rises in value. Is it interest (again, ordinary) income under Code section 1275? These problematic questions reflect the superficial analysis of the IRS's ruling.

The IRS extended the same rationale as was used in Revenue Ruling 95-26 to contributions of short positions to corporate entities in Revenue Ruling 95-45, 1995-1 C.B. 53, issued June 6, 1995. This ruling suffers from the same faulty analysis as was employed in Revenue Ruling 95-26, for the same reasons previously delineated.

In addition to its technical deficiencies, Rev. Rul. 95-26 has questionable pragmatic ramifications. To protect the fisc and perhaps for other policy reasons, the courts and IRS regularly have avoided broad interpretations of partnership liabilities under Code section 752. The uncharacteristically broad interpretation in Rev. Rul. 95-26 has perhaps opened a flood gate for circumventing Code section 731(a) and deferring tax on cash distribu-

tions that otherwise would exceed the basis of a partner's interest. Where a partnership holds a short sale or series of short sales open for an indefinite period of time, the ruling generally would require the inflation of the partners' bases in their partnership interests. The typical aversion by the IRS to the determination that a liability exists for federal income tax purposes is demonstrated by its determination in Rev. Rul. 95- 74, 1995-2 C.B. 36, that contingent environmental liabilities assumed from its parent by a newly created subsidiary of a corporation are not "liabilities" for purposes of Code sections 357(c)(1) and 368. In that ruling, the IRS noted that such contingent liabilities had not yet been taken into account by the parent corporation, and therefore had neither given rise to deductions nor resulted in the creation of, or increase in, basis in any property of the parent. The same reasoning is easily applied to the obligation which arises due to the short sale of securities, and for the same reasons a short sale should not be found to be a liability.

Finally, the unreasonableness of Rev. Rul. 95-26 can be illustrated by analogy to the simple, common transaction of renting a car. Specifically, suppose a calendar-year, accrual method partnership rented a car for a week that overlaps New Year's Day. As in the case of the securities borrower, the partnership is obligated to pay a fee (rent) measured in part by the length of time the property (car) is used. The partnership is also contractually obligated to return the car. Query: which obligation(s) should be treated as partnership liabilities as of year-end—the rent payable upon return of the car or the full value of the car? Curiously, the IRS seems to

suggest that the user record as a partnership liability the full value of the car.

Conclusion

With one exception, that being the March, 1995, revenue ruling, the relevant authorities extending from Rev. Rul. 57-29 to the IRS's litigating position in the cases cited, other than the *Salina* case, consistently oppose treating the borrowing of securities in connection with a short sale as a partnership liability for purposes of Code section 752. The authority for this treatment is substantial, and more likely than not the Company will prevail on this issue if challenged by the IRS.

F. YOUR TAX BASIS IN YOUR INTEREST IN THE COMPANY WILL BE INCREASED BY THE CASH CONTRIBUTED, WITHOUT ADJUSTMENT FOR OBLIGATIONS NOT TREATED AS LIABILITIES FOR TAX PURPOSES

In general, the basis of an interest in a partnership is adjusted for contributions and distributions made by a partner. A partner's tax basis is increased by the amount of money and the adjusted basis of property contributed to the partnership determined as of the date of contribution, and by the amount (if any) of gain recognized to the contributing partner at such time. Code section 722. The basis of a purchased interest is cost. Code section 742; Treas. Reg. sec. 1.742-1. A partner's tax basis is decreased by the amount of money or the adjusted basis of property (other than money) distributed to the partner other than in liquidation of the partnership. Code section 733. If the partnership assumes liabilities of a partner in connection with his contribution of property to the partnership, such decrease in a part-

ner's individual liabilities is deemed to be a distribution of money to the partner by the partnership. Code section 752(b). On the other hand, any increase in a partner's share of liabilities of a partnership or in a partner's individual liabilities by reason of his assumption of partnership liabilities is deemed to be a contribution of money by such partner to the partnership. Code section 752(a). As discussed in Section E, these liabilities more likely than not did not include the borrowing of securities used to effect the short sale.

NOTICE 2000-44 CASE

Internal Revenue Service **Department of the Treasury**

SMALL BUSINESS/
SELF-EMPLOYED DIVISION

4330 WATT AVENUE
SACRAMENTO, CA 95821

CERTIFIED MAIL NUMBER:
7005 0390 0005 1445 4089

Date: [Sept. 07 2006]

ROBERT L. PIERCE
TAX MATTERS PARTNER
POST OFFICE BOX 139
SALISBURY, NC 28145

Refer To:
Pierce, SA 1106
Taxpayer Identifying Number:

Name of Partnership:
HOME CONCRETE & SUPPLY, LLC
Partnership Identifying Number:
56-2136387
Tax Year Ended:
DECEMBER 31, 1999
Date FPAA Mailed to Tax Matters Partner:
[Sept. 7, 2006]
Person to Contact:
Joe Pierce, TEFRA Reviewer
ID 68-10649
Contact Hours:
8:00 am to 4:30 pm
Contact Telephone Number:
(916) 974-5520
Not a toll free number.

NOTICE OF FINAL PARTNERSHIP ADMINISTRATIVE ADJUSTMENT

The law requires us to send a Notice of Final Partnership Administrative Adjustment (FPAA) to the partnership named above, for the tax year shown above, and to each partner who is entitled to receive this notice.

We are proposing adjustments to the partnership items of the partnership and tax year shown above. We will send the examination report outlining these adjustments to the Tax Matters Partner (TMP) of the partnership. (The TMP is the partner designated by the partnership to deal with the IRS.) He/she is also authorized to act for the partners who are not entitled to receive this notice. Any partner who wants a copy of the examination report should request it from the TMP. If the TMP is unable to provide you with a copy of the examination report, please contact the person named in the heading of this letter.

Taxable Years Ending Before August 6, 1997:

The adjustments to the partnership items reported on the partnership tax return may cause an increase or decrease to the tax liability on your individual return. Form 870-P, *Agreement to Assessment and Collection of Deficiency in Tax for Partnership Adjustments*, is a summary of the proposed adjustments to the partnership return. You can compute your share of the proposed adjustments by multiplying each adjusted partnership item by your percentage interest for that partnership item.

Taxable Years Ending After August 5, 1997:

The adjustments to the partnership items reported on the partnership tax return may cause an increase or decrease in the tax liability on your individual return. The adjustments may include partnership level determinations regarding penalties and additions to tax that relate to adjustments to partnership items. Form 870-PT, *Agreement for Partnership Items and Partnership Level Determinations as to Penalties, Additions to Tax, and Additional Amounts*, is a summary of the proposed adjustments to the partnership return. You can compute your share of the proposed adjustments by multiplying each adjusted partnership item by your percentage interest for that partnership item.

You have three options available to you:

1. **If you agree with the adjustments:**

Sign and return the enclosed Form 870-P/Form 870-PT. When you sign Form 870-P/Form 870-PT, you are agreeing to pay any additional tax and interest resulting from the adjustments to the partnership return. For tax years ending after August 5, 1997, you are also agreeing to any partnership level determination as to penalties, additions to tax and additional amounts that relate to adjustments to partnership items, if any. In addition you are waiving your rights to participate in any administrative or judicial proceeding affecting partnership items and in partnership level determinations as to penalties, additions to tax and additional amounts that relate to adjustments to partnership items for the tax year in question. This is a binding settlement only if you sign and return Form 870-P/Form 870-PT and we sign on behalf of the Commissioner of Internal Revenue Service.

When we sign the agreement form, the one-year extension of the period of limitations on assessments will begin under Internal Revenue Code section 6229(f). Once the agreement is signed by both parties, you may not file a claim to change the items in question or claim a refund/credit based on a readjustment.

Note: If you are the TMP of the partnership, see the section of this letter entitled, *"For the Tax Matters Partner of the Partnership"*.

2. If you do not agree with the adjustments:

If you are the TMP of the partnership and want to contest the adjustments in court, you must file a petition within 90 days from the date of this letter. During this 90-day period, no other partner may file a petition for judicial review. You can file your petition for readjustment of partnership items with:

1. the United States Tax Court;
2. the United States Court of Federal Claims; or
3. the District Court of the United States, in the district of the partnership's principal place of business.

A petition filed by the TMP precludes all other actions. If the TMP doesn't file a petition by the 90th day from the date the FPAA was mailed, any partner or any 5 percent group entitled to receive this notice may petition one of these courts. A "five percent group" includes any group of partners who together have an interest of five percent or more in profits of the partnership. The petition must be filed after the 90th day, but on or before the 150th day from the date the FPAA was mailed

to the TMP. If more than one petition is filed in Tax Court, the first petition filed will go forward. All other petitions (even those filed earlier in one of the other courts) will be dismissed. If no one files a petition in Tax Court, the first petition filed in one of the other courts will go forward and subsequent petitions will be dismissed.

Petitions filed with the United States Tax Court must be mailed to:

United States Tax Court
400 Second Street, NW
Washington, DC 20217

Attach a copy of this letter to the petition. The time in which you must file a petition with the court is fixed by law and the court cannot consider your case if your petition is filed late. If this letter is addressed to both husband and wife and both want to petition the Tax Court, both must sign the petition or each must file a separate signed petition.

When a partner (including each member of a 5 percent group that files a petition) files a petition in either the appropriate District Court or the Court of Federal Claims, the partner filing the petition must deposit the amount that the partner's tax liabillity would be increased if the treatment of the partnership items on the partner's return were made consistent with the treatment of partnership items under the FPAA. If you reported the partnership items the way the partnership reported them on its return, you can generally determine the amount to deposit by taking your pro rata share of the partnership adjustments into account in recomputing your tax. You must deposit the appropriate

amount with the IRS on or before the day you file your petition.

3. **If you do nothing:**

If a petition for readjustment is not filed in any of the courts listed in this letter, the FPAA becomes final, and we will bill you for any additional tax plus interest that you may owe under the FPAA. You will not be permitted to contest the treatment of the partnership items of the partnership under the FPAA. You will not be permitted to contest the treatment of the partnership items of the partnership under the FPAA in any refund claim or suit. The law allows the Service to bill you after 150 days from the mailing date of the FPAA to the TMP.

However, if a petition is filed in the Tax Court, and the Tax Court upholds the adjustments in whole or in part, we will not bill you until the Tax Court decision is final.

You may wish to contact the TMP of the partnership or your tax advisor to discuss this matter.

If you have any questions, please write to the person whose name and address are shown in the heading of this letter. If you write, attach a copy of this letter to help identify your account. Also, include your telephone number and the most convenient time for us to call you in case we need additional information.

If you prefer, you may call the IRS contact person at the telephone number shown in the heading of this letter. If this number is outside your local calling area, there will be a long distance charge to you.

Thank you for your cooperation.

Sincerely,
Mark W. Everson
Commissioner, I.R.S.
By:

/s/ TIM CONLEY
TIM CONLEY
Technical Services Territory Manager-West

Enclosures:
Form 870-P/Form 870-PT
Copy of this letter

FOR THE TAX MATTERS PARTNER OF THE PARTNERSHIP

If you are the Tax Matters Partner (TPM), you are entitled to make an agreement to bind non-notice partners to the treatment of the partnership items as shown on the enclosed schedule of adjustments. You must add the following statement above the signature blocks on the Form 870-P or Form 870-PT:

"The undersigned Tax Matters Partner is signing this offer on behalf of himself (herself) and all other partners whom he (she) has the authority to bind; a final agreement resulting from the co-signature of the Commissioner of Internal Revenue will be binding on all such other partners."

As the TMP, you may submit a petition, as described above for the partnership on behalf of all partners.

If you have any questions, you can call the IRS contact person at the telephone number shown in the heading of this letter. Thank you for your cooperation.

Form 870-PT (Rev. 9-2004)	Department of the Treasury — Internal Revenue Service **Agreement for Partnership Items and Partnership Level Determinations as to Penalties, Additions to Tax, and Additional Amounts**	IN REPLY REFER TO: TEFRA Reviewer Phone: 8A 1104

Taxpayer(s) name(s), address and ZIP code:	Name of Partnership: HOME CONCRETE & SUPPLY, LLC	Tax Year(s) Ended:
ROBERT L. PIERCE TAX MATTERS PARTNER POST OFFICE BOX 139 SALISBURY, NC 28145	Taxpayer Identifying Number: 56-2136387	DECEMBER 31, 1999
Taxpayer Identifying Number: 56-2136387	Name of Tax Matters Partner:	

Offer of Agreement to Partnership Items and Partnership Level Determinations as to Penalties, Additions to Tax, and Additional Amounts

&

Waiver of Restrictions on Assessment for Partnership Items, Penalties, Additions to Tax, and Additional Amounts

Under sections 6224(c) and 7121 of the Internal Revenue Code (IRC) of 1986, the Commissioner of the Internal Revenue Service and the undersigned taxpayer(s) agree to the determination of partnership items and partnership level determinations as to penalties, additions to tax, and additional amounts that relate to adjustments to partnership items as shown on the attached schedule of adjustments.

The undersigned taxpayer(s), in accordance with IRC sections 6224(c) and 6213(d), also waive the restrictions provided by IRC sections 6225(a) and 6213(a) and consent to the assessment and collection of any tax attributable to partnership items, penalties, additions to tax, and additional amounts that relate to partnership items, as determined in the agreement, plus any interest provided by law.

This agreement is conditional and will not become effective or final until this agreement form is returned to the Commissioner and is signed on his or her behalf. The one-year extension of the period of limitations on assessments under IRC section 6229(d) will not begin to run until the date the Commissioner's representative signs this form on the Commissioner's behalf. If this is a partial agreement, the period of limitations for assessing any tax attributable to the settled items shall be determined as if this agreement had not been entered into.

If this part of this agreement form is signed for the Commissioner, the treatment of partnership items and partnership level determinations as to penalties, additions to tax and additional amounts that relate to adjustments to partnership items under this agreement will not be reopened in the absence of fraud, malfeasance, or misrepresentation of fact. In addition, no claim for an adjustment of partnership items, refund or credit based on any change in the treatment of partnership items or partnership level determinations as to penalties, additions to tax, and additional amounts may be filed or prosecuted.

Signature of Taxpayer	Date Signed
Signature of Taxpayer	Date Signed
By (Signature and Title)	Date Signed

FOR INTERNAL REVENUE USE ONLY	Date accepted for Commissioner	Signature
	Office	Title

Sep 21 06 08:30p Robert Pierce 910 452 0506 p.5

INSTRUCTIONS FOR SIGNING FORM 870-PT

1. If a JOINT RETURN OF A HUSBAND AND WIFE was filed and both spouses intend to agree, both spouses should sign Form 870-PT. One spouse may sign as agent for the other if acting under a power of attorney, which, if not previously filed, must accompany this form. The IRS may accept the signature of only one spouse at its discretion. However, the agreement will only be binding on the signing spouse.

2. If the taxpayer is a corporation, the waiver must be signed with the corporate name followed by the signature and title of the officer authorized to sign Form 870-PT.

3. Your attorney or agent may sign for you if this action is specifically authorized by a power of attorney, which if not previously filed, must accompany this form.

4. If this offer is signed by a trust, the agreement must be signed with the trust name, followed by the signature and title of the person authorized to sign on behalf of the trust.

5. If this offer is with respect to the tax liability for the consolidated return year, the agreement should be signed in the name of the common parent of the consolidated group for the consolidated return year. The common parent corporation signs the agreement in its own name. The signature and title of a current officer of the common parent corporation, who is authorized to bind the corporation, should be displayed in the signature block.

6. If the Tax Matters Partner signs this offer, please include the title with the signature.

7. If this offer is signed by a Tax Matters Partner that is a subsidiary corporation, then an officer authorized to sign this agreement for the year(s) indicated on the form must sign for the parent corporation. An authorized officer for the subsidiary corporation should also sign if the Tax Matters Partner is binding non-notice partners under the agreement. See Treas. Reg. 1.1502-77(a)(3)(v).

Sep 21 05 08:20p Robert Pierce 310 462 0508 p.8

Department of the Treasury — Internal Revenue Service

Agreement for Partnership Items and Partnership Level Determinations as to Penalties, Additions to Tax, and Additional Amounts

SCHEDULE OF ADJUSTMENTS

NAME OF PARTNERSHIP	TAX YEAR(S) ENDED		
HOME CONCRETE & SUPPLY, LLC	DECEMBER 31, 1999		
TAXPAYER IDENTIFYING NUMBER 68-2136387			
DETAIL OF ADJUSTMENTS TO ORDINARY INCOME			
a. ORDINARY INCOME OR (LOSS) FROM TRADE OR BUSINESS ACTIVITIES			
TOTAL ADJUSTMENTS TO ORDINARY INCOME	$786,282		
OTHER ADJUSTMENTS			
A. CAPITAL CONTRIBUTIONS			
(1) ADJUSTMENT	($16,417,373)		
(2) AS REPORTED	$16,417,373		
(3) CORRECTED	0		
B. DISTRIBUTION OF MONEY			
(1) ADJUSTMENT	($14,618,857)		
(2) AS REPORTED	$14,618,857		
(3) CORRECTED	0		

REMARKS

ACCURACY-RELATED PENALTIES:
- GROSS VALUATION MISSTATEMENT PENALTY
- SUBSTANTIAL VALUATION MISSTATEMENT PENALTY
- NEGLIGENCE PENALTY
- SUBSTANTIAL UNDERSTATEMENT OF INCOME TAX LIABILITY PENALTY

Sep 21 05 08:30p Robert Pierce 918 452 0506 p.7

Form 870-PT, Other Adjustments (Continued)

NAME OF PARTNERSHIP	TAX YEAR(S) ENDED		
HOME CONCRETE & SUPPLY, LLC	DECEMBER 31, 1999		
TAXPAYER IDENTIFYING NUMBER 58-2136367			
C. OUTSIDE PARTNERSHIP BASIS			
(1) ADJUSTMENT	($16,417,373)		
(2) AS REPORTED	$16,417,373		
(3) CORRECTED	0		
D. PORTFOLIO INCOME - INVESTMENT INCOME			
(1) ADJUSTMENT	$97,387		
(2) AS REPORTED	($97,387)		
(3) CORRECTED	0		
E. NET SHORT-TERM CAPITAL GAIN (LOSS)			
(1) ADJUSTMENT	($113,392)		
(2) AS REPORTED	$113,392		
(3) CORRECTED	0		
F. NET LONG-TERM CAPITAL GAIN (LOSS)			
(1) ADJUSTMENT	$182,204		
(2) AS REPORTED	($182,204)		
(3) CORRECTED	0		
G. NET SECTION 1231 GAIN (LOSS)			
(1) ADJUSTMENT	$119,817		
(2) AS REPORTED	($119,817)		
(3) CORRECTED	0		
H. INVESTMENT INCOME INCLUDED ON D. ABOVE			
(1) ADJUSTMENT	($97,387)		
(2) AS REPORTED	$97,387		
(3) CORRECTED	0		
I. ADJUSTMENTS AND TAX PREFERENCE ITEMS - DEPRECIATION			
(1) ADJUSTMENT	($203,833)		
(2) AS REPORTED	$203,833		
(3) CORRECTED	0		

Sep 21 00 08:30p Robert Pierce 910 452 0506 p.8

Form 870-PT, Other Adjustments (Continued)

NAME OF PARTNERSHIP HOME CONCRETE & SUPPLY, LLC TAXPAYER IDENTIFYING NUMBER 58-2136387	TAX YEAR(S) ENDED DECEMBER 31, 1999		
J. ADJUSTMENTS AND TAX PREFERENCE ITEMS - ADJUSTED GAIN OR LOSS			
(1) ADJUSTMENT	$637,849		
(2) AS REPORTED	($637,849)		
(3) CORRECTED	0		
K			
(1) ADJUSTMENT			
(2) AS REPORTED			
(3) CORRECTED			
L			
(1) ADJUSTMENT			
(2) AS REPORTED			
(3) CORRECTED			
M			
(1) ADJUSTMENT			
(2) AS REPORTED			
(3) CORRECTED			
N			
(1) ADJUSTMENT			
(2) AS REPORTED			
(3) CORRECTED			
O			
(1) ADJUSTMENT			
(2) AS REPORTED			
(3) CORRECTED			
P			
(1) ADJUSTMENT			
(2) AS REPORTED			
(3) CORRECTED			

Sep 21 08 08:13p Robert Pierce 810 452 0808 p.3

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	SCHEDULE 2
Name of taxpayer	Tax Identification Number	Year/Period ended
HOME CONCRETE & SUPPLY, LLC	56-2136337	DECEMBER 31, 1999

1. It is determined that neither Home Concrete & Supply, LLC nor its purported partners have established the existence of Home Concrete & Supply, LLC as a partnership as a matter of fact.

2. Even if HOME CONCRETE & SUPPLY, LLC existed as a partnership, the purported partnership was formed and availed of solely for purposes of tax avoidance by artificially overstating basis in the partnership interests of its purported partners. The formation of HOME CONCRETE & SUPPLY, LLC, the acquisition of any interest in the purported partnership by the purported partner, short sales of Treasury Notes,, the transfer of proceeds from short sales of Treasury Notes or other assets to a partnership in return for a partnership interest, the purchase or disposition of assets by the partnership, and the distribution of those assets or proceeds from the disposition of those assets to the purported partners,, and the subsequent sale of those assets to generate a loss, all within a period of less than 8 months, had no business purpose other than tax avoidance, lacked economic substance, and, in fact and substance, constitutes an economic sham for federal income tax purposes. Accordingly, the partnership and the transactions described above shall be disregarded in toll and (1) any purported losses resulting from these transactions are not allowable as deductions; and (2) increases in basis of assets are not allowed to eliminate gain for federal income tax purposes.

3. It is determined that HOME CONCRETE & SUPPLY, LLC was a sham, lacked economic substance and, under § 1.701 2 of the Income Tax Regulations, was formed and availed of in connection with a transaction or transactions in taxable year 1999 a principal purpose of which was to reduce substantially the present value of its partners' aggregate federal tax liability in a manner that is inconsistent with the intent of Subchapter K of the Internal Revenue Code. It is consequently determined that:

a. the HOME CONCRETE & SUPPLY, LLC is disregarded and that all transactions engaged in by the purported partnership are treated as engaged in directly by its purported partners. This includes the determination that the assets purportedly acquired by HOME CONCRETE & SUPPLY, LLC, including but not limited to foreign currency options and Treasury Notes, were acquired directly by the purported partners.

b. the assets and short Treasury Note positions purportedly contributed to or assumed by HOME CONCRETE & SUPPLY, LLC, are treated as never having been contributed to or assumed by said partnership and any gains or losses purportedly realized by HOME CONCRETE & SUPPLY, LLC on the option(s) are treated as having been realized by its partners.
c. the purported partners of HOME CONCRETE & SUPPLY, LLC should be treated as not being partners in HOME CONCRETE & SUPPLY, LLC.
d. contributions to HOME CONCRETE & SUPPLY, LLC will be adjusted to reflect clearly the partnership's or purported partners' income.

4. It is determined that the obligations under the short positions (written call options) transferred to Home Concrete & Supply LLC constitute liabilities for purposes of Treasury Regulation §1.752-6, the assumption of which by Home Concrete & Supply LLC shall reduce the partners' bases in Home Concrete & Supply LLC in the approximate amounts of $70,785, $2,450,000, $2,450,000, and $1,170,000 for Robert L. Pierce, The Pierce Trust A, The Pierce Trust B, and Stephen R. Chandler respectively, but not below the fair market value of the partnership interest.

5. It is determined that the purchased and sold option positions are integrated into a single transaction in accordance with its economic substance under §988.

Sep 21 05 08:32p Robert Pierce 918 492 0508 p.10

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit SCHEDULE 2
Name of taxpayer HOME CONCRETE & SUPPLY, LLC	Tax identification number 36-2136317	Year/Period ended DECEMBER 31, 1999

6. It is determined that neither HOME CONCRETE & SUPPLY, LLC nor its purported partners entered into the option(s) or short sale Treasury Note positions or purchased the foreign currency or stock with a profit motive for purposes of § 165(c)(2).

7. It is also determined the economically offsetting option or short sale Treasury Note positions constitute an arrangement under §465(b)(4) to limit the exposure to risk of loss and that neither HOME CONCRETE & SUPPLY, LLC nor its partners established any other amounts considered to be at risk for purposes of §465 that would allow the partners to deduct losses arising from or in connection with HOME CONCRETE & SUPPLY, LLC.

8. It is determined that, even if the foreign currency option(s) or short sale Treasury Note positions are treated as having been contributed to HOME CONCRETE & SUPPLY, LLC, the amount treated as contributed by the partners under section 722 of the Internal Revenue Code is reduced by the amounts received by the contributing partners from the contemporaneous sales of the call option(s) to the same counter-party. Thus, the basis of the contributed option(s) is reduced, both in the hands of the contributing partners and HOME CONCRETE & SUPPLY, LLC. Consequently, any corresponding claimed increases in the outside basis in HOME CONCRETE & SUPPLY, LLC resulting from the contributions of the foreign currency option(s) are disallowed.

9. It is determined that the adjusted bases of the long call positions (purchased call options), short sale Treasury Note positions, zero coupon notes, and other contributions purportedly contributed by the partners to HOME CONCRETE & SUPPLY, LLC has not been established under I.R.C. § 723. It is consequently determined that the partners of HOME CONCRETE & SUPPLY, LLC have not established adjusted bases in their respective partnership interests in an amount greater than zero (-0-).

10. It is further determined that, in the case of a sale, exchange, or liquidation of HOME CONCRETE & SUPPLY, LLC partners' partnership interests, neither the purported partnership nor its purported partners have established that the bases of the partners' partnership interests were greater than zero for purposes of determining gain or loss to such partners from the sale, exchange, or liquidation of such partnership interest.

11. Under I.R.C. § 752, the amount of the partnership liabilities of Home Concrete & Supply LLC includes aggregate obligations to close open short sales in U.S. Treasury Notes equal to approximately $7,500,000.
a. An increase in a partner's share of partnership liabilities is treated as a contribution of money to the partnership under I.R.C. § 752(a). Under I.R.C. § 722, such a constructive contribution increases a partner's outside basis in his partnership interest. When the short sale obligations were assumed by Home Concrete & Supply LLC, the partnership liabilities of the partnership were increased, and the partners' respective shares of those partnership liabilities were likewise increased, triggering a constructive contribution of cash under I.R.C. § 752(a) that increased their respective outside bases in the partnership under I.R.C. § 722.
b. A decrease in a partner's individual liabilities by reason of the assumption by the partnership of such individual liabilities is treated as a distribution of money to the partner under I.R.C. § 752(b). Under I.R.C. § 733(1), such a constructive distribution reduces a partner's outside basis in their partnership interests. The contribution of the short Treasury Note position, and the assumption by HOME CONCRETE & SUPPLY, LLC of the short sale obligations decreased the individual liabilities of Robert L. Pierce, The Pierce Trust A, The Pierce Trust B, and Stephen R. Chandler, contributing partners, triggering a constructive distribution of cash under I.R.C. § 752(b) that reduced their respective outside bases in HOME CONCRETE & SUPPLY, LLC under I.R.C. § 733(1).

Sep 21 08 08:33p Robert Pierce 310 452 0608 p.11

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit: SCHEDULE 2
Name of taxpayer: HOME CONCRETE & SUPPLY, LLC	Tax identification number: 56-2136387	Year/Period ended: DECEMBER 31, 1999

12. HOME CONCRETE & SUPPLY, LLC filed an IRC Section 754 election to adjust the basis of the assets under IRC Section 743(b). It is determined that there is no excess of outside basis over inside basis. Therefore, the IRC Section 743(b) adjustment to basis is $0 (zero).

13. Accuracy-Related Penalties

It is determined that the adjustments of partnership items of HOME CONCRETE & SUPPLY, LLC are attributable to a tax shelter for which no substantial authority has been established for the position taken, and for which there was no showing of reasonable belief by the partnership or its partners that the position taken was more likely than not the correct treatment of the tax shelter and related transactions. In addition, all of the underpayments of tax resulting from these adjustments of partnership items are attributable to, at a minimum, (1) substantial understatements of income tax, (2) gross valuation misstatement(s), or (3) negligence or disregarded rules or regulations. There has not been a showing by the partnership or any of its partners that there was reasonable cause for any of the resulting underpayments, that the partnership or any of its partners acted in good faith, or that any other exceptions to the penalty apply. It is therefore determined that, at a minimum, the accuracy-related penalty under Section 6662(a) of the Internal Revenue Code applies to all underpayments of tax attributable to adjustments of partnership items of HOME CONCRETE & SUPPLY, L.L.C. The penalty shall be imposed on the components of underpayment as follows:

A. a 40 percent penalty shall be imposed on the portion of any underpayment attributable to the gross valuation misstatement as provided by Sections 6662(a), 6662(b)(3), 6662(e), and 6662(h) of the Internal Revenue Code.
B. a 20 percent penalty shall be imposed on the portion of the underpayment attributable to negligence or disregard of rules and regulations as provided by Sections 6662(a), 6662(b)(1), 6662(c) of the Internal Revenue Code.
C. a 20 percent penalty shall be imposed on the underpayment attributable to the substantial understatement of income tax as provided by sections 6662(a), 6662(b)(2), and 6662(d) of the Internal Revenue Code.
D. a 20 percent penalty shall be imposed on the underpayment attributable to the substantial valuation misstatement as provided by Sections 6662(a), 6662(b)(3), and 6662(e) of the Internal Revenue Code.

It should not be inferred by the determination of the Accuracy Related Penalty in this notice that fraud penalties will not be sought on any portion of an underpayment subsequently determined to be attributable to fraud or that prosecution for criminal offenses will not be sought under IRC § 7201, 7206 or other provisions of federal law if determined to be appropriate.

Sep 21 08 08:33p Robert Pierce 910 452 0508 p.12

UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF
NORTH CAROLINA SOUTHERN DIVISION

No. 7:06-CV-181-FL

HOME CONCRETE & SUPPLY, LLC, A DELAWARE LIMITED LIABILITY COMPANY; ROBERT L. PIERCE, AS TAX MATTERS PARTNER; SUSANNE D. PIERCE; STEPHEN R. CHANDLER; REBECCA R. CHANDLER; AND HOME OIL AND COAL COMPANY, INC., A NORTH CAROLINA CORPORATION, PLAINTIFFS/PETITIONERS

v.

UNITED STATES OF AMERICA,
DEFENDANT/RESPONDENT

[Filed: Mar. 9, 2009]

ORDER

In previous order, the court held in abeyance decision on issues related to whether plaintiffs/petitioners (hereinafter plaintiffs)[1] adequately disclosed information on

---

[1] Plaintiffs include: Home Concrete & Supply, LLC, ("Home Concrete"), a Delaware limited liability company which is deemed a partnership, and its owners who are deemed partners, for federal income tax purposes; Robert L. Pierce ("Pierce"),the tax matters partner for Home Concrete and his wife, plaintiff Susanne D. Pierce, with whom he filed jointly for the 1999 tax year; Stephen R. Chandler ("Chandler"), who proceeds here also with his wife, Rebecca R. Chandler, with whom

their 1999 tax returns to qualify for the safe harbor provision of 26 U.S.C. § 6501(e)(1)(A)(ii), necessary to be decided in considering plaintiffs' motion for summary judgment and motion for partial summary judgment of defendant/respondent (hereinafter defendant). The parties have submitted additional briefing as requested directed to those issues. For the reasons stated below, motion of defendant for partial summary judgment is granted, and plaintiffs' motion for summary judgment is denied.

BACKGROUND

This case involves plaintiffs' reporting of gains from the 1999 sale of their business and related transactions, the details of which are set forth in this court's November 21, 2008 order, incorporated by reference herein. In preparation for the sale of their business, plaintiffs engaged in a series of transactions designed to increase the tax basis in certain business assets. Most notably, plaintiffs conducted short sales of U.S. Treasury Bonds using limited liability companies created especially for this purpose. After opening these short sales, plaintiffs transferred the proceeds from the short sales and the obligations to close them to defendant Home Concrete. Home Concrete immediately closed the short sales. Plaintiffs then sold all of defendant Home Concrete's assets to a third party buyer who is not a party to this case. In reporting their taxable gain from this sale, plaintiffs elected to treat the transfer of the obligation to close the short sales as a non-liability. By so doing,

---

he filed jointly for that tax year; and Home Oil & Coal Company, Inc. ("Home Oil") a North Carolina corporation owned by Pierce and Chandler at the time of its 1999 sale, which is relevant to the instant case.

plaintiffs claimed increased basis in Home Concrete, contending they contributed significant assets (the proceeds of the short sales) to the partnership with no offsetting liability. As a result, they reported a relatively small taxable gain from the subsequent sale of their business.

On September 7, 2006, defendant issued a Notice of Final Partnership Administrative Adjustment ("FPAA") that assessed additional taxes on plaintiffs based on their 1999 returns, asserting plaintiffs' claimed basis increase was improper. Plaintiffs initiated this action to contest the assessment of those additional taxes. The instant motions for summary judgment address the timeliness of the FPAA. In prior order, this court held that the FPAA may be timely because an overstatement of basis can constitute an omission of income for purposes of § 6501(e)(1)(A). However, because there appeared dispute between the parties regarding whether plaintiffs actually overstated basis on their relevant tax returns the court found that it could not address remaining question whether plaintiffs qualified for the "safe harbor" disclosure provision of § 6501(e)(1)(A)(ii). Consequently, the court requested the parties to address in supplemental briefs: (1) whether plaintiffs overstated basis; (2) if so, can the court, on the record before it, now determine whether the resulting omission from gross income was or was not in excess of 25% of the stated gross income amount; and, (3) if it was, whether the safe harbor of § 650l(e)(1)(A)(ii) applies here.

Plaintiffs stipulated, for purposes of resolving the instant motions only, that they "overstated the tax basis of the assets that [Home Concrete] sold in 1999 resulting in an omission of from gross income in excess of 25

percent of the stated gross income amount." (DE# 60 at 2.) Upon this case development, the only remaining issue for the court to address upon these motions is whether plaintiffs sufficiently disclosed information on their relevant tax returns to satisfy the provisions of § 6501(e)(1)(A)(ii).

DISCUSSION

In prior order, this court made two legal determinations that will govern analysis of whether plaintiffs' disclosure was sufficient to qualify for § 650l(e)(1)(A)(ii)'s safe harbor. First, the court found that it may review information contained in both plaintiffs' individual returns and in the relevant partnership returns in determining the adequacy of disclosure. Second, the standard by which plaintiffs' disclosure is to be judged is whether it is "sufficient to indicate what type of item has been omitted and how large (or small) that item is on the face of the relevant returns." Plaintiffs need not have disclosed every precise fact regarding the underlying transactions, however, they "must disclose the substance of a transaction in order to benefit from the shorter limitation period [of § 650l(a)] if the taxpayer omits income."[2] These standards are based on the language of § 650l(e)(1)(A)(ii), which requires disclosure of

---

[2] The "substance" of a transaction, as used by the court, is ultimately synonymous with its "nature." *See* Webster's Third New International Dictionary 2279 (3d ed. 1961) ("1 a: essential nature; essence . . . b: a fundamental part, quality or aspect; essential quality or import: the characteristic and essential part"). Regardless of the precise wording, the ultimate inquiry, as explained below, is whether the item that causes the omission of income is disclosed in substance on the taxpayer's filings.

an omission to include "the nature and amount of such item."

To decide whether the plaintiffs disclosed the "nature and amount" of the underlying, disputed transaction, it is necessary to understand the underlying controversy between the parties. The heart of the parties' dispute is the proper tax treatment of an obligation to close a short sale of treasury notes that partners transfer to a partnership. Plaintiffs Pierce and Chandler opened a series of short sales on U.S. Treasury bonds on May 13, 1999. Four days later, on May 17, 1999, Pierce and Chandler contributed the proceeds of these short sales to defendant Home Concrete, along with the obligation to close the short sales. On May 18, 1999, Home Concrete covered the short sale positions. The plaintiffs' short sale of treasury notes and the accompanying transfer of the short sale proceeds, position, and obligation to close that short sale position to defendant Home Concrete is the transaction that the IRS contends caused the alleged omission of gross income.

Plaintiffs now argue two points regarding adequate disclosure. First, plaintiffs argue that disclosure of a transaction's substance on tax returns for § 6501(e)(1)(A)(ii) should be judged using a reasonableness standard. In other words, the taxpayer should disclose "enough information to reasonably identify the underreporting of gains." (DE# 60 at 6.) Second, they contend the nature of the item omitted that must be reasonably disclosed is merely the election to step-up basis of Home Concrete's assets. This, they argue, is explic-

itly disclosed on Home Concrete's 1999 Form 1065.[3] Plaintiffs further argue that the amount of that step-up in basis was also clearly disclosed on Home Concrete's return as the amount of the step-up adjustment. (Exhibit A to Home Concrete's 1999 Form 1065, DE # 60, Ex. A) Finally, plaintiffs note a number of other disclosures in their various returns, which they allege were sufficient to reasonably apprise the IRS of the omitted amount, when all of the relevant returns are read together.[4]

The government contends that plaintiffs must disclose "the transfer and treatment of their obligation to close the short sales" to qualify for the protection of § 6501(e)(1)(A)(ii). To do this, according to the government, plaintiffs need to have disclosed their treatment of the obligations to close the short sales they transferred to defendant Home Concrete. The government bases its proposed disclosure requirement on the opinions of two other courts to have considered the issue in similar context. *Brandon Ridge Partners v. United States*, 2007 WL 2209129 (M.D. Fla. 2007); *Salman Ranch, Ltd. v. United States*, 79 Fed. Cl. 189 (2007).

As an initial matter, this court finds that a "reasonableness" standard of the sort proposed by plaintiffs to

---

[3] "The partnership hereby elects, under the provisions of Sec. 754 to adjusts [sic] the basis of partnership property in the manner as approved by Sec. 734(b) and Sec. 743(b)." (Attachment to Home Concrete's 1999 Form 1065, DE # 64, Ex. B.)

[4] Specifically, plaintiffs assert that they disclosed: a sale of the assets in the partnership; a sale of U.S. Treasury Bonds on Home Concrete's return; an historically large income for any of the taxpayers involved: and that Home Concrete made more than $8 million in distributions to its partners on its tax return marked as an "initial return."

be appropriate. The Fifth Circuit, the only circuit court to address this issue in a similar context, has adopted such a standard for disclosure, requiring an item omitted from income to be "shown in a manner sufficient to enable the Secretary by reasonable inspection of the return to detect the errors" which form the basis of the omission, in order to be adequately disclosed. *Phinney v. Chambers*, 392 F. 2d 680, 685 (5th Cir. 1968); *Brandon Ridge*, 2007 WL 2209129 at *10.[5] According to the Fifth Circuit, § 6501(e)(1)(A) was designed "to give the Government additional time to investigate tax returns in those cases where a taxpayer's failure to report a taxable item puts the Government at a special disadvantage to discover the omission in the usual three-year period." *Taylor v. United States*, 417 F.2d 991, 993 (5th Cir. 1969)(citing *Colony. Inc. v. Commissioner of Internal Revenue*, 357 U.S. 28 (1958)); *see also CC & F Western Operations Limited Partnership v. Comm'r*, 273 F. 3d 402, 408 (1st Cir. 2001) (noting the purpose of § 6501 is "to give the taxpayer the shorter limitations period where the taxpayer omitted a particular income item from its calculations but disclosed it in substance"). Consequently, if upon inspection of the relevant returns the

---

[5] Surprisingly, plaintiffs criticize the standard used by the court in *Brandon Ridge*, while at the same time arguing for a substantially similar standard. The court in *Brandon Ridge* applied the "reasonably apparent" standard announced by the Fifth Circuit in *Phinney*. Plaintiffs assert that disclosure of the substance of the transaction should consist of "enough information to reasonably identify the underreporting of gains," and argue that they "made more than adequate disclosure sufficient to reasonably apprise the IRS examiner of the 'omission.'" (DE # 60 at 6, 7.) Thus, the standard advocated by plaintiffs appears virtually indistinguishable from the standard they criticize in *Brandon Ridge*.

item is not reasonably apparent, then it has not been adequately disclosed for purposes of § 6501(e)(1)(A)(ii).

The Fifth Circuit's reasonableness standard appears an eminently sensible interpretation of the requirements of § 6501(e)(1)(A)(ii). However, deciding that an item must be reasonably apparent on the face of the relevant returns and their attachments to have been adequately disclosed is only part of the analysis. The question remains what item must be reasonably apparent—put differently, what transaction's substance must be reasonably apparent on plaintiffs' returns. The parties here disagree sharply on this point. Plaintiffs argue that they disclosed the substance of the omitted item by plainly disclosing their election to step-up basis by more than 150% of the basis before the adjustment along with a list of other details that they believe should have alerted the IRS to anything potentially irregular. To require greater disclosure would be, under plaintiffs' argument simply too much of a reporting burden on the average taxpayer.

Plaintiffs' argument here, however, distorts the inquiry. The item omitted in this case is the amount of income not reported by plaintiffs because of the overstatement in basis made by plaintiffs. That overstatement is the error which plaintiffs' disclosure needed to be "reasonably possible for the Secretary to detect." *Phinney*, 392 F.2d at 685. The step-up in basis is part of the error alleged in this case, but only because it is the result of an earlier, allegedly erroneous, election made by plaintiffs in their treatment of the transfer of the short sale obligations from Pierce and Chandler to Home Concrete. Disclosure of an election to step-up basis alone is simply insufficient to apprise the IRS of

the nature of the omission here. There are any number of legitimate ways in which Home Concrete could have claimed a stepped-up basis on its 1999 tax return. Adjusting one's basis for tax purposes is a basic concept under our tax code. Merely disclosing such a stepped-up basis simply cannot form sufficient disclosure to trigger the safe harbor provisions of § 6501(e)(1)(a)(ii) in this situation because such disclosure does not in and of itself "apprise the Secretary" of the alleged error,—namely the allegedly erroneous treatment of the short sale obligations[.] Given that the purpose of § 6501(e) cited above, this court cannot find that such a disclosure is adequate. The nature of the omission here is not simply the election to step-up basis; it is the manner in which plaintiffs generated the alleged basis which allowed them to step-up that basis. To adequately disclose the substance of the transaction, plaintiffs need to have disclosed something on the face of their returns that reasonably apprised the IRS of the disputed election regarding treatment of the obligation to close the short sale.

Review of the documents before this court shows that their disclosure ultimately fails to reveal the substance of this disputed election. To the contrary, plaintiffs' returns contain misleading statements and information that obscured the substance of the disputed underlying transactions. For example, plaintiffs point to two particular statements on their returns, which they assert distinguish their disclosures from those found inadequate in other similar situations. First, they point out that Pierce and Chandler's respective individual tax returns "disclosed a short sale and referred to the obligation to close it," (DE # 60 at 3), through the following state-

ment: "[d]uring the year the proceeds of a short sale not closed by the taxpayer in this tax year were received." (*Id.* at Ex. F, Ex. G.) Second, plaintiffs note that Home Concrete disclosed a large sale of Treasury Bonds on Schedule D of its 1065. (*Id.* at 3, Ex. C.)

Despite plaintiffs' arguments to the contrary, each of these statements is misleading.[6] Nothing about the disclosure on Pierce and Chandler's individual tax returns reasonably indicates that the opening of the short sales was related to the basis step-up by Home Concrete. Quite to the contrary, this "disclosure" actually masks the ultimate purpose of those short sales. The statement on Pierce and Chandler's tax returns indicates that those taxpayers retained the obligation to close the short sales they had opened. There is no hint that either taxpayer had transferred the obligation to close the short sale. The logical inference from this disclosure is exactly the opposite. Such misdirection cannot form the basis of adequate disclosure.

Plaintiff's revelation of a sale of Treasury Bonds in Home Concrete's Schedule D also serves as a smokescreen for plaintiffs' actual activities. In Part I, column (a) of Home Concrete's Schedule D, plaintiffs disclosed "1. Sale of US Treasury Bonds." In column (b), plaintiffs listed the date on which these treasury bonds were acquired as May 18, 1999 and listed the date sold in col-

---

[6] Plaintiffs argue that the mere mention of a short sale in Pierce and Chandler's individual returns is sufficient to distinguish the facts of this case from those in *Brandon Ridge* and *Salman Ranch* and to render their disclosure adequate. But simply reporting the opening of a short sale on plaintiffs' individual tax returns does not reveal the substance of their basis election or the transactions behind it. Further, as discussed here, the wording of plaintiffs' disclosure is misleading at best.

umn (c) as May 19, 1999. The sales price listed in column (d) was $7,472,405.00 and the basis was listed as $7,359,043.00 in column (e), producing a column (f) gain of $113,362.00. Viewing this disclosure alone reveals nothing of the actual nature of the transaction. The description of the sale itself is completely misleading. Plaintiffs did not disclose a "short sale" of Treasury Bonds or the "close of a short sale position," nor did they use any other descriptive moniker that accurately described the transaction.[7] Instead, they rather mislead-

---

[7] Plaintiffs argue that requiring greater disclosure than they provided here would somehow impose a great burden on taxpayers. This court finds no merit to plaintiff's argument. Nothing in this court's opinion requires plaintiffs or similarly situated taxpayers to "attach[ ] to the return the short sale paperwork, the Jenkens opinion letters, or other justification for taking the basis adjustment" as plaintiffs seem to assert. (DE # 60 at 8.) To the contrary, adequate disclosure in this case could have been made from the face of the returns with a few additions and corrections. For example, had plaintiffs correctly identified the short sale of Treasury Bonds on Home Concrete's Schedule D, they may have had a strong claim to adequate disclosure. Plaintiffs instead chose to omit the crucial descriptive word "short" in their reporting, making it into the misleading statement included in their documentation before the court. This is not to say that such a change alone would have been adequate disclosure, but it is to say that adequate disclosure is not as burdensome as plaintiffs argue.

Plaintiffs also argue that their disclosure of the short sales on their individual returns should be adequate because normally there is no tax effect to opening a short sale position and, therefore, there is no need to report such an opening. As such, plaintiffs assert that their advisers understood that reading all of the returns together would adequately disclose what plaintiffs were doing. Regardless of what plaintiffs' advisers understood about required disclosure, what they advised plaintiffs to disclose, and what plaintiffs actually disclosed, are misleading statements and details that, though connected in reality, do not appear connected in plaintiffs' returns, precisely because of how plaintiffs chose to phrase and structure their disclosure.

ingly indicated that Home Concrete engaged in a "sale of U.S. Treasury Bonds" in which it ostensibly made $113,362.00 in one day. The dates listed by plaintiffs only serve to reinforce the notion that they were reporting a straight sale of Treasury Bonds instead of the back-end of a short sale transaction. Plaintiffs listed an acquisition date of May 18, 1999, and a sale date of May 19, 1999. Regardless of whether this was a fair representation of the actual events that occurred on those days, when paired with the statement "1. Sale of US Treasury Bonds," the only reasonable conclusion a reviewer was likely to draw was that Home Concrete engaged in a straight sale of Treasury Bonds on the dates in question.

Viewing these two disclosures together does not reveal the substance of the disputed transaction. Nothing on the face of the returns connects these two disclosures together in a way that indicates that they were, in fact, the opening and closing of the same short sale transaction. Pierce and Chandler's individual returns indicate they each opened a short sale, received the proceeds from it, and did not close that short sale in the 1999 tax year. Implicit in this "disclosure" is that Pierce and Chandler retained the short sale position and the obligation to close that short sale, which was not actually the case. Home Concrete's return simply states that the partnership obtained Treasury Bonds and sold them one day later, earning a profit from the transaction. There is no hint anywhere in Home Concrete's Form 1065 that Home Concrete received a short sale position from Pierce and Chandler and proceeded to close it. Had there been such any indication that Home Concrete did indeed close a short sale, plaintiffs may have had a

strong case that they had adequately disclosed the substance of the alleged error here and may have qualified for the safe harbor provision of § 6501(e)(1)(A)(ii).[8] However, as it stands, putting these two disclosures side-by-side the substance of the disputed election is not reasonably apparent, and even an IRS examiner trained in the art of divination would have been hard pressed to discern plaintiffs' true actions.

None of the other items highlighted by plaintiffs improve the adequacy of their disclosure in light of the misleading details discussed above. For example, plaintiffs argue that from the face of their returns, it is apparent: (1) that each partner engaged in a short sale that was not closed; (2) that the partnership received a large infusion of cash; (3) the partnership engaged in a large sale of U.S. Treasury Bonds; (4) that such sale was followed by an enormous step-up in basis; (5) that such step-up preceded the sale of Home Concrete's business

---

[8] This court need not, and does not, decide whether such a disclosure alone would suffice for purposes of that provision. However, the potential ease of making such a disclosure in this case eviscerates plaintiffs' complaints that the disclosures now required by this court would be unduly burdensome. Had plaintiffs disclosed on their Form 1065 Schedule D a "Short Sale of U.S. Treasury Bonds," they would have taken a large step closer toward adequate disclosure. Had plaintiffs coupled such a disclosure on Home Concrete's return together with disclosure on Pierce and Chandler's individual returns that Pierce and Chandler received and transferred the proceeds of short sales along with the obligation to close those short sales to Home Concrete, plaintiffs would have been, at the very least, straddling the line between adequate and inadequate disclosure. Because this question is not before the court, it does not decide whether such disclosure would have been adequate. It does, however, find that such disclosure would have been closer to adequate than the inadequate disclosures made by plaintiffs in this case.

assets; and (6) that the partnership made a large distribution to its partners with very little gain flowing through to them. These disclosures, however, do not reasonably disclose the disputed means by which plaintiffs made their step-up in basis. Arguably, taken together, these disclosures could be sufficient to make an IRS examiner curious enough to flag plaintiffs' returns for an audit. However, the standard for disclosure is not whether the taxpayer's return contains enough suspicious details to trigger an audit. The standard is whether the taxpayer disclosed "nature and amount" of the alleged omission at issue. This court has already held that to disclose the nature and amount of an omission of income caused by an overstatement of basis, the taxpayer must disclose the substance of the transaction that created the overstatement. Plaintiffs' disclosures in this case fail to do that and, as already discussed, actually make discerning the true nature of the plaintiffs' alleged error and the item allegedly omitted more difficult. Consequently, plaintiffs' disclosures do not qualify for the safe harbor provision of § 6501(e)(1)(A)(ii), and the government's action is timely under the six-year statute of limitations prescribed by § 6501(e).

CONCLUSION

For the foregoing reasons, the defendant's motion for partial summary judgment is GRANTED and the plaintiffs' motion for summary judgment is DENIED. Accordingly, pursuant to this court's previous order entered on October 9, 2007, the parties shall submit a Joint Status Report by March 23, 2009, proposing an expeditious schedule for the conduct of any further discovery, and requested trial dates. If further settlement activities may prove beneficial, this information also shall be

reported. A magistrate judge may be made available to facilitate a court-hosted settlement conference if requested.

SO ORDERED, this the [9th] day of March, 2009.

/s/ LOUISE W. FLANAGAN
Chief United States District Judge

UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA

No. 7:06-CV-00181-FL

HOME CONCRETE & SUPPLY, LLC, ET AL.,
PLAINTIFFS

v.

UNITED STATES OF AMERICA, DEFENDANT

Thursday, Aug. 6, 2009
9:00 a.m.

DEPOSITION OF ROBERT L. PIERCE

---

[7]

* * * * *

that at one point you were considering a divorce. Are you still married to the lady who was your wife at the time?

A. No, I'm not.

Q. All right. Is she represented by counsel in this matter in Federal Court?

A. No.

Q. She's not a part of the proceeding at all?

A. No.

Q. During the time you were married, did she participate in any way in the meetings and other events we've been discussing in depositions as they relate to the transaction with Jenkens & Gilchrist?

A. No, she didn't.

Q. I notice she did sign some documents. Did she have any role beyond that?

A. No, that was all she did.

Q. Beg your pardon?

A. That was all she did.

Q. All right. After you graduated in 1968, I'll focus on that period, '68 to—is it 1985 when you came to Home Oil?

A. No, I was—state that again.

Q. I'll rephrase the question. When did you first come to Home Oil?

[8]

A. When I was 13 years old. It was a family business. I used to bag coal there.

Q. Okay. Did you have any employment any place besides Home Oil after you graduated college?

A. No, I did not.

Q. Okay. And did you start working there shortly after you graduated?

A. The day after.

Q. What did you do in the company at that point?

A. We were just getting into the concrete business. We had been in the heating oil and coal business, and I went to work mainly in the concrete part of our business selling, learning about concrete, that sort of thing.

Q. Who was—

MR. RICE: Did you finish?

A. Yeah, I'm finished.

BY MR. HARTT:

Q. Who was running the company at that point?

A. My mother was President of the company, and Steve Chandler's dad was Vice President and the two of them ran the company.

Q. Was it Bruce Chandler?

A. Bruce Chandler?

Q. Is that Steve Chandler's dad?

[9]

A. No. I don't know a Bruce Chandler.

Q. Besides you and your mother, were there any other family members who were a part of the operation?

A. No.

Q. All right. You mentioned that about the time you began working there after college there was a shift from the coal and the oil business more into the concrete business.

A. That's correct. Although, we were still in the oil and coal business also.

Q. Was there a point in time where you basically got out of the coal and oil business?

A. Yes.

Q. When did that happen?

A. Probably some time in the early '90s we quit selling coal all together because that market was gone. The oil business, which we were mainly in the heating oil business, we had also sold gasoline to some small mom and pop stations, convenience stores, but not the type you see today, and that business was kind of going away. We were looking for something else to do, and we ended up in the concrete business. But the year we sold the business we sold what was left of the oil business, which amounted to three or four trucks and some tanks, sold it to a man that was in the country, had an oil business in the [10] county. He just bought our equipment and customers.

Q. Did you also, besides the concrete business, move into like building supplies?

A. We worked our way into that over the years. I mean, it's—we were a small company trying to grow, and we started selling—I mean, we had dump trucks. So we started selling masonry sand and mortar mix and stuff like that, and over the years we ended up being a full service building supply dealer.

Q. When you began in 1968, about how many employees did the company have?

A. 15 at the most.

Q. And by the time the business sold in 1999, how many employees did you have?

A. In the upper 40s.

Q. In 1968 how many buildings, physical plants, I'm not sure the best word to describe it, but how many different locations did you have?

A. One.

Q. All right. By the time you had sold the business in 1999, had that changed?

A. One.

Q. You would have I guess some offices as part of this facility.

A. We had a warehouse that we stored building

* * * * *

[17]

A. No, I was not.

Q. But you ultimately became a shareholder at one point?

A. That's correct.

Q. About what point in time?

A. I don't know what year. My mother gave me some stock over time each year, gave my sister some. In 1985—and Steve's dad had done the same for him and his other siblings. So in 1985 he was ready to retire. My mom was not working much, but still had not—still

owned the majority of the business and was somewhat ready to retire. So Steve and I bought out their interest and paid for it over a 15 year period.

Q. So you bought out your sister's interest and you bought out his sib—

A. We bought—the company, as well as I remember, I'm not sure exactly how it worked. I don't remember. But we paid—we bought and paid for the shares that everybody owned. Steve's brothers and sisters—brother and sister, and my sister, we bought their shares and paid for them. Then we paid for—we paid for my mother's and Mr. Chandler's, Steve's dad's, shares with a note paid over 15 years.

Q. During the process in which you acquired the other shares, did the percentage of the company owned by [18] the Pierce family, a percentage owned by the Chandler family, did that change at all?

A. Yes it did.

Q. You acquired a larger share?

A. Yes, I ended up with a larger share. The share that my mother originally owned was 75 percent and Steve's dad 25 percent. And when we bought back the shares from everybody and what was left, I ended up with 81 point something percent and Steve 18 point something percent.

Q. And this process you said began in 1985—

A. Yes.

Q. —and covered a 15 year period, which would have gotten us to the year 2000, which is the year after the company was sold.

A. That's correct, made the last payment in April of 2000. I think that's correct.

Q. I've seen references in the documents here to a Thomas Chandler, and for the reference he's no relation to Steve Chandler. Is that correct?

A. That's correct.

Q. Just a coincidence of last name?

A. Yeah, just a coincidence.

Q. Could you also help me—there is a Central Concrete, which I think acquired your business in 1999.

* * * * *

[91]

A. I don't remember.

Q. Would you expect that you did?

A. I would.

MR. RICE: Objection.

BY MR. HARTT:

Q. You would?

A. I suspect I saw it, but I don't know and remember that I provided the answers.

MR. HARTT: Let's go off the record.

(A lunch break was taken)

BY MR. HARTT:

Q. All right. Let's go back on the record. Mr. Pierce, I think you testified this morning that the first meeting you had with Arthur Andersen was the one in Greensboro on March the 9th.

A. That's correct.

Q. What had led you to Arthur Andersen?

A. I had been thinking about selling our company. I was getting on up in age a little bit. My children weren't interested in coming back to Salisbury working 14 hours a day like the old man had been. So in thinking of selling the business, and I had had people knocking on the doors. The big concrete companies around were buying out a lot of us little guys. We had one plant in one [92] town, and the big companies have them all over the place and they were buying a lot of concrete companies. And so I had some interest, and I knew that would go away one of these days when the construction cycle turned the other way as they do go up and down.

So I talked to a banker that I had known that had made a lot of money in the last few years through—his bank had gone public, and there had been three or four mergers and I knew he had made some money like that. So I asked him and thought he probably had gotten financial help somewhere. So I saw him at the bank one day and told him that I was trying to do some financial planning. I didn't tell him I was thinking about selling the business, because I didn't want a rumor to get started in small Salisbury, and told him I was trying to do some financial planning for the future and that sort of thing, and did he have any suggestions of who I might

talk to, and he gave me Tim Boyle's name with Arthur Andersen.

Q. And you subsequently called up Mr. Boyle, and that let at some point to the meeting?

A. That's right. I called Mr. Boyle and told him that I had an interest in selling a business and I needed help to value that business. I didn't want to value it or put a price tag out that was too cheap and give it [93] away or put out one that was too high to scare people off. And, also, that I would need some help with, well, that's more money than I've ever seen. You know, how do we best handle that tax wise, investment wise, that sort of thing.

So we set up a meeting, and he said, as far as selling the business, I suggest you use Lloyd & Company. They're an investment bank right here in Greensboro, and I know those folks. So he lined up the meeting, and I went to Greensboro. That's how we got started.

Q. Were there representatives of Lloyd at the meeting on March the 9th?

A. Yes, Ken Wiles with Lloyd & Company was there.

Q. Was he there on March the 17th, the next meeting you had, the one in Charlotte?

A. Yes. I don't recall for sure, but he might have been. I started having—and I don't really remember whether he was there or not because I started having a lot of meetings with him as well as Arthur Andersen folks.

Q. Did you seek recommendations from anybody else on who you might consult with?

A. No, I did not.

Q. Once you had the recommendation for Arthur [94] Andersen, did you make any attempt to check up on them, into their record, reputation or anything like that?

A. No, I didn't. When you think of Arthur Andersen—and I knew that name. I knew it doesn't get any better than that or didn't think it did. In fact, I was a little bit concerned about calling them because I thought I was probably too small for them to pay me any attention.

Q. At the meeting on March the 9th, was there any discussion of a program to minimize the taxes on the sale of the company?

A. We talked about or they talked about, yes, there are ways to save some taxes.

Q. Did they mention anything to you about Jenkens & Gilchrist?

A. I don't recall that they did.

Q. Now, between the meeting on March the 9th and the meeting in Charlotte on March the 17th, did you have any phone calls or correspondence with anyone at Arthur Andersen.

A. I would have talked to either Nancy or Tim Boyle about the meeting on the 17th to get it lined up I'm sure, and they may have asked me for some information about our company, about me and that sort of thing.

Q. Prior to your meeting on March the 17th, had [95] any of them mentioned Jenkens & Gilchrist to you?

A. I don't recall.

Q. Is your best recollection then it was the meeting on the 17th when you first heard of Jenkens & Gilchrist?

A. That's the first conversation I had involving them. Whether they mentioned them to me in that, between the 9th and the 17th, I don't remember, or on the 9th for that matter.

Q. At whatever point during this period of time you heard somebody mention Jenkens & Gilchrist to you, had you previously heard of this law firm?

A. No, sir.

Q. Once you had heard of it and—did you hear about Mr. Mayer individually at the same time?

A. Yes.

Q. Did you make any effort to look into the background of either the firm or him individually?

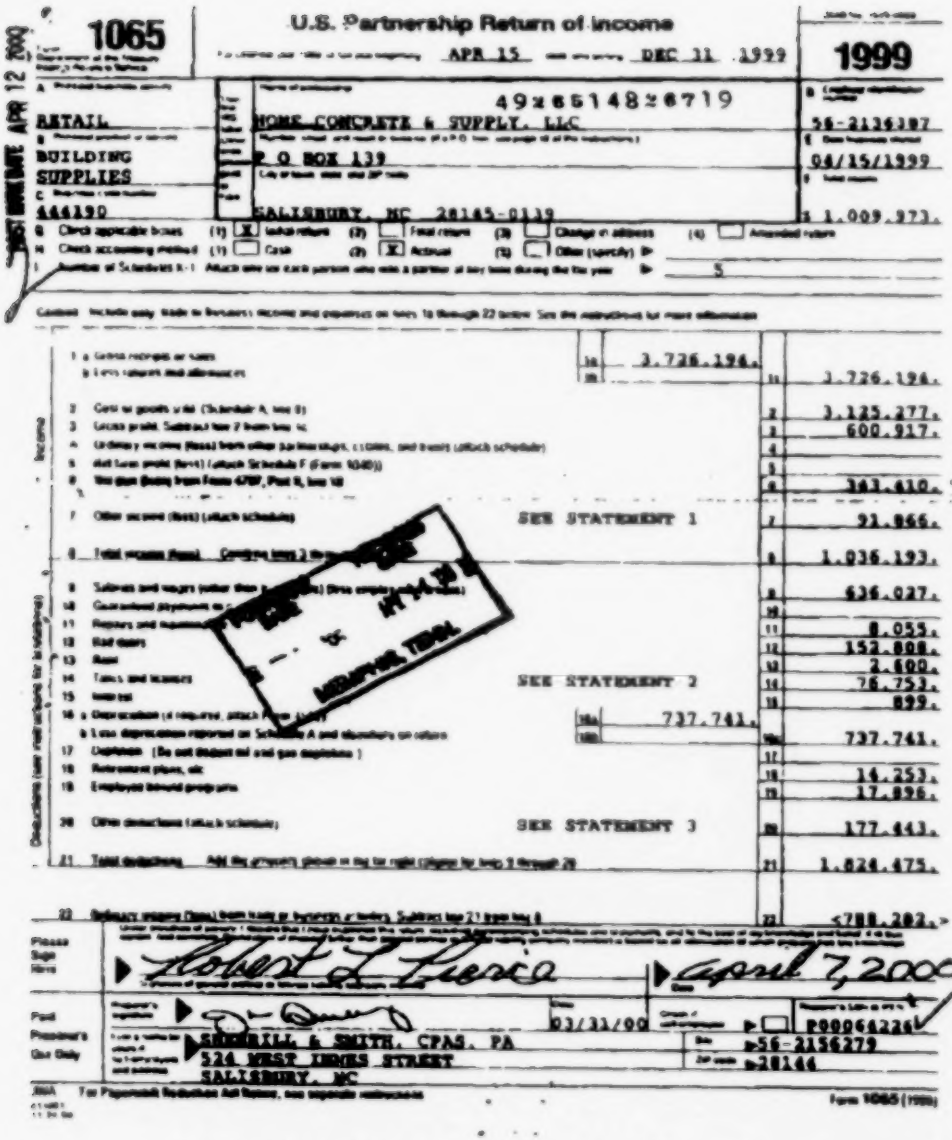
A. No sir, I didn't. I thought that if Arthur Andersen was dealing with them, then I didn't need to, didn't even cross my mind.

Q. So you didn't ask about how long he had been practicing law?

A. No.

Q. Where he went to law school?

* * * * *



Form 1065 — U.S. Partnership Return of Income — 1999

IRS RECEIVED APR 12 2000

APR 15 — DEC 31 1999

A RETAIL BUILDING SUPPLIES — 444190

49-65514826719

HOME CONCRETE & SUPPLY, LLC

P O BOX 139

SALISBURY, NC 28145-0139

B 56-2136387

C 04/15/1999

D $ 1,009,973.

G Check applicable boxes: (1) [X] Initial return (2) [ ] Final return (3) [ ] Change of address (4) [ ] Amended return

H Check accounting method: (1) [ ] Cash (2) [X] Accrual (3) [ ] Other (specify)

I Number of Schedules K-1: Attach one for each person who was a partner at any time during the tax year ▶ 5

Income	1a Gross receipts or sales	1a 3,726,194.		
	b Less returns and allowances	1b	1c	3,726,194.
	2 Cost of goods sold (Schedule A, line 8)		2	3,125,277.
	3 Gross profit. Subtract line 2 from line 1c		3	600,917.
	4 Ordinary income (loss) from other partnerships, estates, and trusts (attach schedule)		4	
	5 Net farm profit (loss) (attach Schedule F (Form 1040))		5	
	6 Net gain (loss) from Form 4797, Part II, line 18		6	343,410.
	7 Other income (loss) (attach schedule)	SEE STATEMENT 1	7	91,866.
	8 Total income (loss). Combine lines 3 through 7		8	1,036,193.
Deductions (see instructions for limitations)	9 Salaries and wages (other than to partners) (less employment credits)		9	636,027.
	10 Guaranteed payments to partners		10	
	11 Repairs and maintenance		11	8,055.
	12 Bad debts		12	152,808.
	13 Rent		13	2,600.
	14 Taxes and licenses	SEE STATEMENT 2	14	76,753.
	15 Interest		15	899.
	16a Depreciation (if required, attach Form 4562)	16a 737,741.		
	b Less depreciation reported on Schedule A and elsewhere on return	16b	16c	737,741.
	17 Depletion (Do not deduct oil and gas depletion.)		17	
	18 Retirement plans, etc.		18	14,253.
	19 Employee benefit programs		19	17,896.
	20 Other deductions (attach schedule)	SEE STATEMENT 3	20	177,443.
	21 Total deductions. Add the amounts shown in the far right column for lines 9 through 20		21	1,824,475.
	22 Ordinary income (loss) from trade or business activities. Subtract line 21 from line 8		22	<788,282.>

Please Sign Here: Robert L Fierce — April 7, 2000

Paid Preparer's Use Only: Preparer's signature — Date 03/31/00 — Check if self-employed [ ] — Preparer's SSN or PTIN P00064226

SHERRILL & SMITH, CPAS, PA — 524 WEST INNES STREET — SALISBURY, NC — EIN ▶56-2156279 — ZIP code ▶28144

For Paperwork Reduction Act Notice, see separate instructions. — Form 1065 (1999)

RECEIVED APR 12 2000 CLERK U.S. DIST. COURT MEMPHIS, TENN.

Form 1065 (1999) HOME CONCRETE & SUPPLY, LLC 56-2136387 Page 3

Schedule A Cost of Goods Sold

1	Inventory at beginning of year	1	881,200.
2	Purchases less cost of items withdrawn for personal use	2	2,244,077.
3	Cost of labor	3	
4	Additional section 263A costs (attach schedule)	4	
5	Other costs (attach schedule)	5	
6	Total. Add lines 1 through 5	6	3,125,277.
7	Inventory at end of year	7	
8	Cost of goods sold. Subtract line 7 from line 6. Enter here and on page 1, line 2	8	3,125,277.

9a Check all methods used for valuing closing inventory

(i) ☐ Cost as described in Regulations section 1.471-3

(ii) ☒ Lower of cost or market as described in Regulations section 1.471-4

(iii) ☐ Other (specify method used and attach explanation) ▶

b Check this box if there was a write-down of "subnormal" goods as described in Regulations section 1.471-2(c) ▶ ☐

c Check this box if the LIFO inventory method was adopted this tax year for any goods (if checked, attach Form 970) ▶ ☐

d Do the rules of section 263A (for property produced or acquired for resale) apply to the partnership? ☐ Yes ☒ No

e Was there any change in determining quantities, cost, or valuations between opening and closing inventory? ☐ Yes ☒ No

If "Yes," attach explanation

Schedule B Other Information

		Yes	No
1	What type of entity is filing this return? Check the applicable box:		
	a ☐ General partnership b ☐ Limited partnership c ☒ Limited liability company		
	d ☐ Limited liability partnership e ☐ Other ▶		
2	Are any partners in this partnership also partnerships?		X
3	Is this partnership a partner in another partnership?		X
4	Is this partnership subject to the consolidated audit procedures of sections 6221 through 6233? If "Yes," see Designation of Tax Matters Partner below		X
5	Does this partnership meet ALL THREE of the following requirements?		
	a The partnership's total receipts for the tax year were less than $250,000;		
	b The partnership's total assets at the end of the tax year were less than $600,000; AND		
	c Schedules K-1 are filed with the return and furnished to the partners on or before the due date (including extensions) for the partnership return.		
	If "Yes," the partnership is not required to complete Schedules L, M-1, and M-2, item F on page 1 of Form 1065; or item J on Schedule K-1		X
6	Does this partnership have any foreign partners?		X
7	Is this partnership a publicly traded partnership as defined in section 469(k)(2)?		X
8	Has this partnership filed, or is it required to file, Form 8264, Application for Registration of a Tax Shelter?		X
9	At any time during the calendar year 1999, did the partnership have an interest in or a signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account)? (See the instructions for exceptions and filing requirements for Form TD F 90-22.1.) If "Yes," enter the name of the foreign country. ▶		X
10	During the tax year, did the partnership receive a distribution from, or was it the grantor of, or transferor to, a foreign trust? If "Yes," the partnership may have to file Form 3520 or 926. See page 10 of the instructions.		X
11	Was there a distribution of property or a transfer (e.g., by sale or death) of a partnership interest during the tax year? If "Yes," you may elect to adjust the basis of the partnership's assets under section 754 by attaching the statement described under Elections Made by the Partnership	X	

Designation of Tax Matters Partner

Enter below the general partner designated as the tax matters partner (TMP) for the tax year of this return:

Name of designated TMP ▶ ROBERT L PIERCE

Identifying number of TMP ▶ [redacted]

Address of designated TMP ▶ 400 NORTH LONG STREET
SALISBURY, NC 28144

Form 1065 (1999)

12210331 767285 1233 1999.05200 HOME CONCRETE & SUPPLY, LLC 1233 1

HOME CONCRETE & SUPPLY, LLC 56-2136387

Schedule K Partners' Shares of Income, Credits, Deductions, etc.

		(a) Distributive share items		(b) Total amount
Income (Loss)	1	Ordinary income (loss) from trade or business activities	1	<788,282.>
	2	Net income (loss) from rental real estate activities	2	
	3a	Gross income from other rental activities	3a	
	b	Expenses from other rental activities	3b	
	c	Net income (loss) from other rental activities	3c	
	4	Portfolio income (loss):		
	a	Interest income SEE STATEMENT 4	4a	<97,387.>
	b	Ordinary dividends	4b	
	c	Royalty income	4c	
	d	Net short-term capital gain (loss)	4d	113,262.
	e	Net long-term capital gain (loss)	4e(2)	<152,286.>
	f	Other portfolio income (loss)	4f	
	5	Guaranteed payments to partners	5	
	6	Net section 1231 gain (loss)	6	<110,817.>
	7	Other income (loss)	7	
Deductions	8	Charitable contributions	8	
	9	Section 179 expense deduction	9	
	10	Deductions related to portfolio income	10	
	11	Other deductions	11	
Credits	12a	Low-income housing credit		
		(1) From partnerships to which section 42(j)(5) applies for property placed in service before 1990	12a(1)	
		(2) Other than on line 12a(1) for property placed in service before 1990	12a(2)	
		(3) From partnerships to which section 42(j)(5) applies for property placed in service after 1989	12a(3)	
		(4) Other than on line 12a(3) for property placed in service after 1989	12a(4)	
	b	Qualified rehabilitation expenditures related to rental real estate activities	12b	
	c	Credits related to rental real estate activities	12c	
	d	Credits related to other rental activities	12d	
	13	Other credits	13	
Investment Income and Investment Expenses	14a	Interest expense on investment debts	14a	
	b	(1) Investment income included on lines 4a, 4b, 4c, and 4f above	14b(1)	<97,387.>
		(2) Investment expenses included on line 9 above	14b(2)	
Self-Employment	15a	Net earnings (loss) from self-employment	15a	0.
	b	Gross farming or fishing income	15b	
	c	Gross nonfarm income	15c	
Adjustments and Tax Preference Items	16a	Depreciation adjustment on property placed in service after 1986	16a	293,833.
	b	Adjusted gain or loss SEE STATEMENT 6	16b	<637,849.>
	c	Depletion (other than oil and gas)	16c	
	d	(1) Gross income from oil, gas, and geothermal properties	16d(1)	
		(2) Deductions allocable to oil, gas, and geothermal properties	16d(2)	
	e	Other adjustments and tax preference items	16e	
Foreign Taxes	17a	Type of income		
	b	Name of foreign country or U.S. possession		
	c	Total gross income from sources outside the United States	17c	
	d	Total applicable deductions and losses	17d	
	e	Total foreign taxes (check one) Paid Accrued	17e	
	f	Reduction in taxes available for credit	17f	
	g	Other foreign tax information	17g	
Other	18	Section 59(e)(2) expenditures	18b	
	19	Tax-exempt interest income	19	
	20	Other tax-exempt income	20	
	21	Nondeductible expenses SEE STATEMENT 5	21	345.
	22	Distributions of money (cash and marketable securities)	22	$ 6,693,414.
	23	Distributions of property other than money	23	
	24	Other items and amounts required to be reported separately to partners		

Form 1065 (1999)

12210331 767285 1233 1999.05200 HOME CONCRETE & SUPPLY, LLC 1233 1

Form 1065 (1999) HOKE CONCRETE & SUPPLY, LLC 56-2116387 Page 4

Analysis of Net Income (Loss)

1 Net income (loss). Combine Schedule K, lines 1 through 7 in column (a). From the result, subtract the sum of Schedule K, lines 8 through 11, 14a, 17b, and 18b					1	<1,045,328.>
2 Analysis by partner type:	(i) Corporate	(ii) Individual (active)	(iii) Individual (passive)	(iv) Partnership	(v) Exempt organization	(vi) Nominee/Other
a General partners						
b Limited partners	<1,041,032.>		<869.>			<3,427.>

Schedule L Balance Sheets per Books (Not required if Question 5 on Schedule B is answered "Yes.")

Assets	Beginning of tax year (a)	Beginning of tax year (b)	End of tax year (c)	End of tax year (d)
1 Cash				9,971.
2a Trade notes and accounts receivable				
b Less allowance for bad debts				
3 Inventories				
4 U.S. government obligations				
5 Tax-exempt securities				
6 Other current assets (attach schedule)	STATEMENT 8			1,000,000.
7 Mortgage and real estate loans				
8 Other investments (attach schedule)				
9a Buildings and other depreciable assets				
b Less accumulated depreciation				
10a Depletable assets				
b Less accumulated depletion				
11 Land (net of any amortization)				
12a Intangible assets (amortizable only)				
b Less accumulated amortization				
13 Other assets (attach schedule)				
14 Total assets		0.		1,009,971.
Liabilities and Capital				
15 Accounts payable				
16 Mortgages, notes, bonds payable in less than 1 year				
17 Other current liabilities (attach schedule)	STATEMENT 9			259,614.
18 All nonrecourse loans				
19 Mortgages, notes, bonds payable in 1 year or more				
20 Other liabilities (attach schedule)				
21 Partners' capital accounts				750,359.
22 Total liabilities and capital		0.		1,009,973.

Schedule M-1 Reconciliation of Income (Loss) per Books With Income (Loss) per Return (Not required if Question 5 on Schedule B is answered "Yes." See page 25 of the instructions.)

1 Net income (loss) per books	<1,048,147.	6 Income recorded on books this year not included on Schedule K, lines 1 through 7 (itemize): a Tax-exempt interest $	
2 Income included on Schedule K, lines 1 through 4, 6, and 7, not recorded on books this year (itemize):			
3 Guaranteed payments (other than health insurance)		7 Deductions included on Schedule K, lines 1 through 11, 14a, 17b, and 18b, not charged against book income this year (itemize): a Depreciation $	
4 Expenses recorded on books this year not included on Schedule K, lines 1 through 11, 14a, 17b, and 18b (itemize): a Depreciation $			
b Travel and entertainment $ 345. STMT 11 2,674.	2,819.	8 Add lines 6 and 7	
5 Add lines 1 through 4	<1,045,328.>	9 Income (loss) (Analysis of Net Income (Loss), line 1). Subtract line 8 from line 5	<1,045,328.>

Schedule M-2 Analysis of Partners' Capital Accounts (Not required if Question 5 on Schedule B is answered "Yes.")

1 Balance at beginning of year		6 Distributions: a Cash STMT 7	14,618,867.
2 Capital contributed during year STMT 13	16,417,373.	b Property	
3 Net income (loss) per books	<1,048,147.>	7 Other decreases (itemize):	
4 Other increases (itemize):		8 Add lines 6 and 7	14,618,867.
5 Add lines 1 through 4	15,369,226.	9 Balance at end of year. Subtract line 8 from line 5	750,359.

Form 1065 (1999)

SCHEDULE D (Form 1065)

Department of the Treasury
Internal Revenue Service

Name of partnership

Capital Gains and Losses

▶ Attach to Form 1065

OMB No 1545-0099

1999

Employer identification number

HOME CONCRETE & SUPPLY, LLC

56-2136287

Part I Short-Term Capital Gains and Losses - Assets Held 1 Year or Less

(a) Description of property (Ex. 100 shares of "Z" Co.)	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Sales price	(e) Cost or other basis	(f) Gain or (loss) ((d) minus (e))
1 SALE OF US TREASURY BONDS	05/18/99	05/19/99	7,472,405.	7,359,043.	113,362.

2 Short-term capital gain from installment sales from Form 6252, line 26 or 37	2	
3 Short-term capital gain or (loss) from like-kind exchanges from Form 8824	3	
4 Partnership's share of net short-term capital gain (loss), including specially allocated short-term capital gains (losses), from other partnerships, estates, and trusts	4	
5 Net short-term capital gain or (loss). Combine lines 1 through 4 in column (f). Enter here and on Form 1065, Schedule K, line 4a, or 7	5	113,362.

Part II Long-Term Capital Gains and Losses - Assets Held More Than 1 Year

(a) Description of property (Ex. 100 shares of "Z" Co.)	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Sales price	(e) Cost or other basis	(f) Gain or (loss) ((d) minus (e))	(g) 28% rate gain or (loss) * - Long gain Author
6 SALE OF GOODWILL	VARIOUS	08/31/99	9,201,472.	9,355,461.	<153,989.>	
SALE OF IRRA STOCK	VARIOUS	08/31/99		8,215.	<8,215.>	

7 Long-term capital gain from installment sales from Form 6252, line 26 or 37	7	
8 Long-term capital gain (loss) from like-kind exchanges from Form 8824	8	
9 Partnership's share of net long-term capital gain (loss), including specially allocated long-term capital gains (losses), from other partnerships, estates, and trusts	9	
10 Capital gain distributions	10	
11 Combine lines 6 through 10 in column (g). Enter here and on Form 1065, Schedule K, line 4a(1) or 7	11	
12 Net long-term capital gain or (loss). Combine lines 6 through 10 in column (f). Enter here and on Form 1065, Schedule K, line 4a(2) or 7	12	<162,204.>

* 28% rate gain or (loss) includes all "collectibles gains and losses" as defined in the instructions.

JSA For Paperwork Reduction Act Notice, see the instructions for Form 1065. Schedule D (Form 1065) 1999

12210331 767285 1233 1999.05200 HOME CONCRETE & SUPPLY, LLC 1233___1

DOJ-018156

SCHEDULE K-1 (Form 1065)

Partner's Share of Income, Credits, Deductions, etc.

For calendar year 1999 or tax year beginning APR 15, 1999 and ending DEC 31, 1999

1999

Partner's identifying number ▶ 56-0546791

Partner's name, address, and ZIP code

HOKE OIL & COAL COMPANY, INC
P O BOX 139
SALISBURY, NC 28145-0139

Partnership's identifying number ▶ 56-2136387

Partnership's name, address, and ZIP code

HOKE CONCRETE & SUPPLY, LLC
P O BOX 139
SALISBURY, NC 28145-0139

A This partner is a [ ] general partner [ ] limited partner [X] limited liability company member

B What type of entity is this partner? ▶ S CORPORATION

C Is this partner a [X] domestic or a [ ] foreign partner?

D Enter partner's percentage of:

	Before change or termination	End of year
Profit sharing	98.2700000%	99.9827000%
Loss sharing	98.2700000%	99.9827000%
Ownership of capital	98.2700000%	92.7941066%

E Partner's share of liabilities:

Nonrecourse	$
Qualified nonrecourse financing	$
Other	$ 0.

F Tax shelter registration number ▶

G Check here if this partnership is a publicly traded partnership as defined in section 469(k)(2) [ ]

H Check applicable boxes: (1) [ ] Final K-1 (2) [ ] Amended K-1

I Enter partner's beginning and ending percentages:

(a) Capital account at beginning of year	(b) Capital contributed during year	(c) Partner's share of lines 1, 4, and 7, Form 8865, Schedule M-2	(d) Withdrawals and distributions	(e) Capital account at end of year (combine columns (a) through (d))
	10,272,847.	<1,043,840.>	8,532,718.	696,289.

	(a) Distributive share item	(b) Amount	(c) 1040 filers enter the amount in column (b) on
Income (Loss)	1 Ordinary income (loss) from trade or business activities	<705,042.>	See page 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	2 Net income (loss) from rental real estate activities		
	3 Net income (loss) from other rental activities		
	4 Portfolio income (loss): a Interest	<96,987.	Sch. B, Part I, line 1
	b Ordinary dividends		Sch. B, Part II, line 5
	c Royalties		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	112,896.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss): (1) 28% rate gain (loss)		Sch. D, line 12, col. (g)
	(2) Total for year	<161,537.	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)		Enter on applicable line of other return
	5 Guaranteed payments to partner		See page 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	6 Net sec. 1231 gain (loss) (other than casualty or theft)	<110,362.	
	7 Other income (loss) (attach schedule)		Enter on applicable line of your return
Deductions	8 Charitable contributions (attach schedule)		Sch. A, line 15 or 16
	9 Section 179 expense deduction		See page 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	10 Deductions related to portfolio income (attach schedule)		
	11 Other deductions (attach schedule)		
Credits, Investment Interest & SE	12 Other credits		Enter on applicable line of your return
	13 a Interest expense on investment debts		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	<96,987.	See page 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	(2) Investment expenses included on line 10 above		
	14 a Net earnings (loss) from self-employment		Sch. SE, Section A or B
	b Gross farming or fishing income		See page 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	c Gross nonfarm income		
Adjustments & Tax Preference Items	15 a Depreciation adjustment on property placed in service after 1986	202,995.	See Partner's Instructions for Schedule K-1 (Form 1065) and Instructions for Form 6251
	b Adjusted gain or loss SEE STATEMENT	<635,227.>	
	c Other adjustments and tax preference items (attach schedule)		
Other	16 Tax-exempt interest income		Form 1040, line 8b
	17 Other tax-exempt income		See pages 3 and 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	18 Nondeductible expenses SEE STATEMENT	344.	
	19 Distributions of money (cash and marketable securities)	8,532,718.	
	20 Distributions of property other than money		

For Paperwork Reduction Act Notice, see Form 1065 instructions. No information Required for Page 2 Schedule K-1 (Form 1065) 1999

INTEREST ON U.S. OBLIGATIONS INCLUDED IN LINE 4A <113,737.>

12210331 767285 1233 1999.05300 HOKE CONCRETE & SUPPLY, LLC 1233 1

HOME CONCRETE & SUPPLY, LLC 56-2136387

SCHEDULE K-1 CAPITAL CONTRIBUTED DURING THE YEAR

DESCRIPTION	AMOUNT
CONTRIBUTIONS TO CAPITAL	4,347,394.
TRANSFERRED CAPITAL	5,925,453.
TOTAL TO SCHEDULE K-1, ITEM J, COLUMN B	10,272,847.

SCHEDULE K-1 NONDEDUCTIBLE EXPENSES

DESCRIPTION	AMOUNT	PARTNER INSTRUCTIONS
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	344.	NONDEDUCTIBLE PORTION
TOTAL TO SCHEDULE K-1, LINE 21	344.	

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	PARTNER INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<635,227.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 16B	<635,227.>		

SCHEDULE K-1 (Form 1065)

Partner's Share of Income, Credits, Deductions, etc.

For calendar year 1999 or tax year APR 15, 1999 and ending DEC 31, 1999

1999

Partner's identifying number [redacted]

Partnership's employer identification number ▶ 56-2136387

Partner's name, address, and ZIP code

ROBERT L PIERCE
[redacted]
SALISBURY, NC

Partnership's name, address, and ZIP code

HOME CONCRETE & SUPPLY, LLC
P O BOX 139
SALISBURY, NC 28145-0139

A This partner is a [ ] general partner [ ] limited partner
[X] limited liability company member

B What type of entity is this partner? ▶ INDIVIDUAL

C Is this partner a [X] domestic or a [ ] foreign partner?

D Enter partner's percentage of:

	(i) Beginning of tax year	(ii) End of tax year
Profit sharing	0.0200000%	0.0002000%
Loss sharing	0.0200000%	0.0002000%
Ownership of capital	0.0200000%	0.0034081%

E IRS Center where partnership filed return: MEMPHIS, TN

F Partner's share of liabilities:

Nonrecourse	$
Qualified nonrecourse financing	$
Other	$ 0.

G Tax shelter registration number ▶

H Check here if this partnership is a publicly traded partnership as defined in section 469(k)(2) [ ]

I Check applicable boxes: (1) [ ] Final K-1 (2) [ ] Amended K-1

J Analysis of partner's capital account:

(a) Capital account at beginning of year	(b) Capital contributed during year	(c) Partner's share of lines 1, 2, and 7, Form 1065, Schedule M-2	(d) Withdrawals and distributions	(e) Capital account at end of year (combine columns (a) through (d))
	70,785.	<49.>	70,110.	626.

	(a) Distributive share item	(b) Amount	(c) 1040 filers enter the amount in column (b) on
Income (Loss)	1 Ordinary income (loss) from trade or business activities	<37.>	See page 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	2 Net income (loss) from rental real estate activities		
	3 Net income (loss) from other rental activities		
	4 Portfolio income (loss): a Interest	<4.>	Sch. B, Part I, line 1
	b Ordinary dividends		Sch. B, Part II, line 5
	c Royalties		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	5.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss): (1) 28% rate gain (loss)		Sch. D, line 12, col. (g)
	(2) Total for year	<8.>	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)		Enter on applicable line of your return
	5 Guaranteed payments to partner		See page 4 of Partner's Instructions for Schedule K-1 (Form 1065)
	6 Net sec. 1231 gain (loss) (other than casualty or theft)	<5.>	
	7 Other income (loss) (attach schedule)		Enter on applicable line of your return
Deductions	8 Charitable contributions (attach schedule)		Sch. A, line 15 or 16
	9 Section 179 expense deduction		See page 7 and 8 of Partner's Instructions for Schedule K-1 (Form 1065)
	10 Deductions related to portfolio income (attach schedule)		
	11 Other deductions (attach schedule)		
Credits, Investment Interest & SE	12 Other credits		Enter on applicable line of your return
	13 a Investment interest expense		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	<4.>	See page 8 of Partner's Instructions for Schedule K-1 (Form 1065)
	(2) Investment expenses included on line 13a above		
	14 a Net earnings (loss) from self-employment	0.	Sch. SE, Section A or B
	b Gross farming or fishing income		See page 8 of Partner's Instructions for Schedule K-1 (Form 1065)
	c Gross nonfarm income		
Adjustments & Tax Items	15 a Depreciation adjustment on property placed in service after 1986	10.	See Partner's Instructions for Schedule K-1 (Form 1065) and Instructions for Form 6251
	b Adjusted gain or loss SEE STATEMENT	<31.>	
	c Other adjustments and tax preference items (attach schedule)		
Other	16 Tax-exempt interest income		Form 1040, line 8b
	17 Other tax-exempt income		See pages 8 and 10 of Partner's Instructions for Schedule K-1 (Form 1065)
	18 Nondeductible expenses		
	19 Distributions of money (cash and marketable securities)	1,609.	
	20 Distributions of property other than money		

JMA For Paperwork Reduction Act Notice, see Form 1065 instructions. See Information Required for Page 3 Schedule K-1 (Form 1065) 1999

INTEREST ON U.S. OBLIGATIONS INCLUDED IN LINE 4A <5.>

2

12210331 767285 1233 1999.05200 HOME CONCRETE & SUPPLY, LLC 1233 1

ROME CONCRETE & SUPPLY, LLC 56-2136387

SCHEDULE K-1 WITHDRAWALS AND DISTRIBUTIONS

DESCRIPTION	AMOUNT
CASH DISTRIBUTION	1,609.
TRANSFERRED CAPITAL	68,501.
TOTAL TO SCHEDULE K-1, ITEM J, COLUMN D	70,110.

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	PARTNER INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<31.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 16B	<31.>		

SCHEDULE K-1 (Form 1065)

Partner's Share of Income, Credits, Deductions, etc.

For calendar year 1999 or tax year beginning APR 15, 1999 and ending DEC 31, 1999

OMB No. 1545-0099

1999

Partner's identifying number [redacted]

Partnership's identifying number ▶ 56-2136387

Partner's name, address, and ZIP code

[redacted]
SALISBURY, NC

Partnership's name, address, and ZIP code

HOME CONCRETE & SUPPLY, LLC
P O BOX 139
SALISBURY, NC 28145-0139

A This partner is a [ ] general partner [ ] limited partner
[X] limited liability company member

B What type of entity is this partner? ▶ INDIVIDUAL

C Is this partner a [X] domestic or a [ ] foreign partner?

D Enter partner's percentage of:

	(i) Share of profit, loss or interest	(ii) Share of capital or interest
Profit sharing	0.3300000%	0.0033000%
Loss sharing	0.3300000%	0.0033000%
Ownership of capital	0.3300000%	1.3745247%

E Partner's share of liabilities:

Nonrecourse	$
Qualified nonrecourse financing	$
Other	$ 0.

F Tax shelter registration number ▶

G Check here if this partnership is a publicly traded partnership as defined in section 469(k)(2) [ ]

H Check applicable boxes: (1) [ ] Final K-1 (2) [ ] Amended K-1

I Partner's share of partnership's nonrecourse liabilities at year end

J Partner's share of partnership's beginning capital account

(a) Capital account at beginning of year	(b) Capital contributed during year	(c) Partner's share of lines 1, 4, and 7, Form 1065, Schedule M-2	(d) Withdrawals and distributions	(e) Capital account at end of year (combine columns (a) through (d))
	1,171,957.	<822.>	(1,160,821.)	10,314.

	(a) Distributive share item	(b) Amount	(c) 1040 filers enter the amount in column (b) on:
Income (Loss)	1 Ordinary income (loss) from trade or business activities	<618.>	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	2 Net income (loss) from rental real estate activities		
	3 Net income (loss) from other rental activities		
	4 Portfolio income (loss): a Interest	<77.	Sch. B, Part I, line 1
	b Ordinary dividends		Sch. B, Part II, line 5
	c Royalties		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	89.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss): (1) 28% rate gain (loss)		Sch. D, line 12, col. (g)
	(2) Total for year	<127.	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)		Enter on applicable line of your return
	5 Guaranteed payments to partner		
	6 Net section 1231 gain (loss) (other than casualty or theft)	<87.>	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	7 Other income (loss) (attach schedule)		Enter on applicable line of your return
Deductions	8 Charitable contributions (attach schedule)		Sch. A, line 15 or 16
	9 Section 179 expense deduction		See page 7 of Partner's Instructions for Schedule K-1 (Form 1065)
	10 Deductions related to portfolio income (attach schedule)		
	11 Other deductions (attach schedule)		Enter on applicable line of your return
Credits, Investment Interest & SE	12 Other credits		
	13 a Interest expense on investment debts		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	<77.	See page 8 of Partner's Instructions for Schedule K-1 (Form 1065)
	(2) Investment expenses included on line 10 above		
	14 a Net earnings (loss) from self-employment	0.	Sch. SE, Section A or B
	b Gross farming or fishing income		See page 8 of Partner's Instructions for Schedule K-1 (Form 1065)
	c Gross nonfarm income		
Adjustments & Tax Preference Items	15 a Depreciation adjustment on property placed in service after 1986	160.	See Partner's Instructions for Schedule K-1 (Form 1065) or Instructions for Form 6251
	b Adjusted gain or loss SEE STATEMENT	<500.	
	c Other adjustments and tax preference items (attach schedule)		
Other	16 Tax-exempt interest income		Form 1040, line 8b
	17 Other tax-exempt income		See page 8 of Partner's Instructions for Schedule K-1 (Form 1065)
	18 Nondeductible expenses		
	19 Distributions of money (cash and marketable securities)	10,533.	
	20 Distributions of property other than money		

JSA For Paperwork Reduction Act Notice, see Form 1065 instructions. See Information Required for Page 2 Schedule K-1 (Form 1065) 1999

INTEREST ON U.S. OBLIGATIONS INCLUDED IN LINE 4A <90.>

12210331 767285 1233 1999.05200 HOME CONCRETE & SUPPLY, LLC 1233 3

HOME CONCRETE & SUPPLY, LLC 56-2136387

SCHEDULE K-1 WITHDRAWALS AND DISTRIBUTIONS

DESCRIPTION	AMOUNT
CASH DISTRIBUTION	30,533.
TRANSFERRED CAPITAL	1,130,288.
TOTAL TO SCHEDULE K-1, ITEM J, COLUMN D	1,160,821.

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	PARTNER INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<500.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 16B	<500.>		

SCHEDULE K-1 (Form 1065)

Partner's Share of Income, Credits, Deductions, etc.

For calendar year 1999 or tax year beginning APR 15, 1999 and ending DEC 31, 1999

1999

Partner's identifying number ▶ 58-6388592

Partner's name, address, and ZIP code

THE 1999 ROBERT L PIERCE GRANTOR
TRUST A FBO JULIE M PIERCE
310 BETHEL DRIVE
SALISBURY, NC 28144

Partnership's identifying number ▶ 56-2136387

Partnership's name, address, and ZIP code

HOME CONCRETE & SUPPLY, LLC
P O BOX 139
SALISBURY, NC 28145-0139

A This partner is a [ ] general partner [ ] limited partner
[X] limited liability company member

B What type of entity is this partner? ▶ TRUST

C Is this partner a [X] domestic or a [ ] foreign partner?

D Enter partner's percentage of:

	(i) Before change or termination	(ii) End of year
Profit sharing	0.6900000%	0.0069000%
Loss sharing	0.6900000%	0.0069000%
Ownership of capital	0.6900000%	2.8739803%

E Partner's share of liabilities:

Nonrecourse	$
Qualified nonrecourse financing	$
Other	$ 0.

F Tax shelter registration number ▶

G Check here if this partnership is a publicly traded partnership as defined in section 469(k)(2) [ ]

H Check applicable boxes: (1) [ ] Final K-1 (2) [ ] Amended K-1

I Analysis of partner's capital account:

(a) Capital account at beginning of year	(b) Capital contributed during year	(c) Partner's share of income, gain, loss, Form 1065, Schedule M-2	(d) Withdrawals and distributions	(e) Capital account at end of year (combine columns (a) through (d))
2,450,892.		<1,718.>	2,427,609.	21,565.

	(a) Distributive share item	(b) Amount	(c) 1040 filers enter the amount in column (b) on
Income (Loss)	1 Ordinary income (loss) from trade or business activities	<1,293.>	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	2 Net income (loss) from rental real estate activities		
	3 Net income (loss) from other rental activities		
	4 Portfolio income (loss): a Interest	<160.	Sch. B, Part I, line 1
	b Ordinary dividends		Sch. B, Part II, line 5
	c Royalties		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	186.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss): (1) 28% rate gain (loss)		Sch. D, line 12, col. (g)
	(2) Total for year	<266.	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)		Enter on applicable line of your return
	5 Guaranteed payments to partner		See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	6 Net sec. 1231 gain (loss) (other than casualty or theft)	<181.	
	7 Other income (loss) (attach schedule)		Enter on applicable line of your return
Deductions	8 Charitable contributions (attach schedule)		Sch. A, line 15 or 16
	9 Section 179 expense deduction		
	10 Deductions related to portfolio income (attach schedule)		See page 7 and 8 of Partner's Instructions for Schedule K-1 (Form 1065)
	11 Other deductions (attach schedule)		
Credits, Investment Interest, SE	12 Other credits		Enter on applicable line of your return
	13 a Interest expense on investment debts		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	<160.	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	(2) Investment expenses included on line 10 above		
	14 a Net earnings (loss) from self-employment		Sch. SE, Section A or B
	b Gross farming or fishing income		See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	c Gross nonfarm income		
Adjustments and Tax Preference	15 a Depreciation adjustment on property placed in service after 1986	334.	See Partner's Instructions for Schedule K-1 (Form 1065) and Instructions for Form 6251
	b Adjusted gain or loss SEE STATEMENT	<1,045.>	
	c Other adjustments and tax preference items (attach schedule)		
Other	16 Tax-exempt interest income		Form 1040, line 8b
	17 Other tax-exempt income		See page 6 and 10 of Partner's Instructions for Schedule K-1 (Form 1065)
	18 Nondeductible expenses		
	19 Distributions of money (cash and marketable securities)	64,277.	
	20 Distributions of property other than money		

JSA For Paperwork Reduction Act Notice, see Form 1065 instructions. See Information Required for Page 7 Schedule K-1 (Form 1065) 1999

INTEREST ON U.S. OBLIGATIONS INCLUDED IN LINE 4A <187.>

12210331 767285 1233 1999.05200 HOME CONCRETE & SUPPLY, LLC 1233 1

HOME CONCRETE & SUPPLY, LLC 56-2136387

SCHEDULE K-1 WITHDRAWALS AND DISTRIBUTIONS

DESCRIPTION	AMOUNT
CASH DISTRIBUTION	64,277.
TRANSFERRED CAPITAL	2,363,332.
TOTAL TO SCHEDULE K-1, ITEM J, COLUMN D	2,427,609.

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	PARTNER INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<1,045.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 16B	<1,045.>		

SCHEDULE K-1 (Form 1065) — Partner's Share of Income, Credits, Deductions, etc. — 1999

For calendar year 1999 or tax year beginning APR 15, 1999 and ending DEC 31, 1999

Partnership's identification number ▶ 56-2116387

Partnership's name, address, and ZIP code:
HOME CONCRETE & SUPPLY, LLC
P O BOX 139
SALISBURY, NC 28145-0139

IRS Center where partnership filed return: MEMPHIS, TN

Partner's identifying number ▶ 58-6388593

Partner's name, address, and ZIP code:
THE 1999 ROBERT L PIERCE GRANTOR
TRUST B FBO ROBERT C PIERCE
310 BETHEL DRIVE
SALISBURY, NC 28144

A This partner is a [ ] general partner [ ] limited partner
[X] limited liability company member

B What type of entity is this partner? ▶ TRUST

C Is this partner a [X] domestic or a [ ] foreign partner?

D Enter partner's percentage of:

	(i) Beginning of tax year	(ii) End of tax year
Profit sharing	0.6200000%	0.0069000%
Loss sharing	0.6900000%	0.0069000%
Ownership of capital	0.6900000%	2.8739803%

E Partner's share of liabilities:

Nonrecourse	$
Qualified nonrecourse financing	$
Other	$ 0.

F Tax shelter registration number ▶

G Check here if this partnership is a publicly traded partnership as defined in section 469(k)(2) [ ]

H Check applicable boxes: (1) [ ] Final K-1 (2) [ ] Amended K-1

I Analysis of partner's capital account:

(a) Capital account at beginning of year	(b) Capital contributed during year	(c) Partner's share of income (see page 7 of Form 1065, Schedule M-2)	(d) Withdrawals and distributions	(e) Capital account at end of year (combine columns (a) through (d))
3,458,892.		<1,718.>	2,427,609.	31,565.

	(a) Distributive share item	(b) Amount	(c) 1040 filers enter the amount in column (b) on:
Income (Loss)	1 Ordinary income (loss) from trade or business activities	<1,292.>	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	2 Net income (loss) from rental real estate activities		
	3 Net income (loss) from other rental activities		
	4 Portfolio income (loss): a Interest	<159.>	Sch. B, Part I, line 1
	b Ordinary dividends		Sch. B, Part II, line 5
	c Royalties		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	186.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss): (1) 28% rate gain (loss)		Sch. D, line 12, col. (g)
	(2) Total for year	<266.>	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)		Enter on applicable line of your return
	5 Guaranteed payments to partner		
	6 Net sec. 1231 gain (loss) (other than casualty or theft)	<182.>	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	7 Other income (loss) (attach schedule)		Enter on applicable line of your return
Deductions	8 Charitable contributions (attach schedule)		Sch. A, line 15 or 16
	9 Section 179 expense deduction		
	10 Deductions related to portfolio income (attach schedule)		See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	11 Other deductions (attach schedule)		
Credits, Investment Interest & SE	12 Other credits		
	13 a Interest expense on investment debts		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	<159.>	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	(2) Investment expenses included on line 10 above		
	14 a Net earnings (loss) from self-employment		Sch. SE, Section A or B
	b Gross farming or fishing income		See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	c Gross nonfarm income		
Adjustments and Tax Preference	15 a Depreciation adjustment on property placed in service after 1986	314.	See Partner's Instructions for Schedule K-1 (Form 1065) and Instructions for Form 6251
	b Adjusted gain or loss SEE STATEMENT	<1,046.>	
	c Other adjustments and tax preference items (attach schedule)		
Other	16 Tax-exempt interest income		Form 1040, line 8b
	17 Other tax-exempt income		
	18 Nondeductible expenses SEE STATEMENT	1.	See page 6 of Partner's Instructions for Schedule K-1 (Form 1065)
	19 Distributions of money (cash and marketable securities)	64,277.	
	20 Other property distributions		

JSA For Paperwork Reduction Act Notice, see Form 1065 instructions. No Information Required for Page 2 Schedule K-1 (Form 1065) 1999

INTEREST ON U.S. OBLIGATIONS INCLUDED IN LINE 4A <187.>

12210331 767285 1233 1999.05200 HOME CONCRETE & SUPPLY, LLC 1233 1

HOME CONCRETE & SUPPLY, LLC 56-2136387

SCHEDULE K-1 WITHDRAWALS AND DISTRIBUTIONS

DESCRIPTION	AMOUNT
CASH DISTRIBUTION	64,277.
TRANSFERRED CAPITAL	2,363,332.
TOTAL TO SCHEDULE K-1, ITEM J, COLUMN D	2,427,609.

SCHEDULE K-1 NONDEDUCTIBLE EXPENSES

DESCRIPTION	AMOUNT	PARTNER INSTRUCTIONS
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	1.	NONDEDUCTIBLE PORTION
TOTAL TO SCHEDULE K-1, LINE 21	1.	

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	PARTNER INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<1,046.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 16B	<1,046.>		

Form **4797** — **Sales of Business Property**

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

▶ Attach to your tax return.

1999

Attachment Sequence No. **27**

BOSE CONCRETE & SUPPLY, LLC — 56-2136387

1 Enter the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or substitute statement) that you are including on line 2, 10, or 20 — 1

Part I Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft - Property Held More Than 1 Year

(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2 SALE OF BUILDINGS						
	VARIES	083199	2340000.	406,518.	2,818,745.	<72,227.>
SALE OF LAND						
	VARIES	083199	95,000.		133,590.	<38,590.>

3	Gain, if any, from Form 4684, line 39	3
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5
6	Gain, if any, from line 32, from other than casualty or theft	6
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows:	7 <110,817.>
	Partnerships (except electing large partnerships). Report the gain or (loss) following the instructions for Form 1065, Schedule K, lines 9 and 10. Skip lines 8, 9, 11, and 12 below. S corporations. Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax. All others. If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	
8	Nonrecaptured net section 1231 losses from prior years (see instructions)	8
9	Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line as follows (see instructions): S corporations. Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below. All others. If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D.	9

Part II Ordinary Gains and Losses

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

SALE OF INVENTORY & RECEIVABLES						
	VARIES	083199	3179587.		3,332,523.	<152,936.>

11	Loss, if any, from line 7	11
12	Gain, if any, from line 7 or amount from line 8, if applicable	12
13	Gain, if any, from line 31	13 496,346.
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations (see instructions)	17
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18 343,410.
a	For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.	
b	For individual returns:	
(1)	If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)." See instructions	18b(1)
(2)	Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)

JSA For Paperwork Reduction Act Notice, see separate instructions. Form 4797 (1999)

HOME CONCRETE & SUPPLY, LLC

56-2136387

Part III Gain From Dispositions of Property Under Sections 1245, 1250, 1252, 1254, and 1255

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:

A SALE OF BULK PLANT TANKS & PUMPS — VARIES 082499

B SALE OF BUILDING SUPPLY EQUIPMENT — VARIES 083199

C SALE OF CONCRETE BATCH PLANT — VARIES 083199

D SALE OF FURNITURE & FIXTURES — VARIES 083199

These columns relate to the properties on lines 19A through 19D		Property A	Property B	Property C	Property D
20 Gross sales price (Note. See line 1 before completing.)	20	1,500.	155,017.	271,500.	104,004.
21 Cost or other basis plus expense of sale	21	20,079.	342,902.	701,804.	299,591.
22 Depreciation (or depletion) allowed or allowable	22	19,845.	220,869.	453,476.	207,864.
23 Adjusted basis. Subtract line 22 from line 21	23	234.	121,133.	248,328.	91,727.
24 Total gain. Subtract line 23 from line 20	24	1,266.	33,884.	23,172.	12,277.
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	19,845.	220,869.	453,476.	207,864.
b Enter the smaller of line 24 or 25a	25b	1,266.	33,884.	23,172.	12,277.
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	496,346.
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	496,346.
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

See instructions

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See instructions for where to report	35		

HOME CONCRETE & SUPPLY, LLC 56-2136387

Form 4797 (1999) Page 2

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A SALE OF RADIOS & RADIO EQUIPMENT	VARIES	083199
B SALE OF REDI MIX TRUCKS	VARIES	083199
C SALE OF VEHICLES-SALES	VARIES	083199
D SALE OF VEHICLES-SHOP	VARIES	083199

Please complete relevant to the properties on lines 19A through 19D.		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20	30,491.	731,109.	46,500.	20,500.
21 Cost or other basis plus expense of sale	21	90,854.	2,161,699.	104,071.	61,257.
22 Depreciation (or depletion) allowed or allowable	22	80,338.	1,697,657.	58,647.	44,134.
23 Adjusted basis. Subtract line 22 from line 21	23	10,516.	466,042.	45,424.	19,123.
24 Total gain. Subtract line 23 from line 20	24	19,975.	265,058.	1,076.	1,377.
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	80,338.	1,697,657.	58,647.	44,134.
b Enter the smaller of line 24 or 25a	25b	19,975.	265,058.	1,076.	1,377.
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D, line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See the instructions for where to report	35		

HOME CONCRETE & SUPPLY, LLC 56-2136187

Form 4797 (1998) Page 2

Part III Gain From Dispositions of Property Under Sections 1245, 1250, 1252, 1254, and 1255

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A SALE OF BUILDING SUPPLY TRUCKS	VARIES	083199
B SALE OF REDI-MIX EQUIPMENT	VARIES	083199
C SALE OF SHOP EQUIPMENT	VARIES	083199
D		

These columns relate to the properties on lines 19A through 19D		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20	261,000.	160,500.	26,676.	
21 Cost or other basis plus expense of sale	21	687,292.	294,511.	35,952.	
22 Depreciation (or depletion) allowed or allowable	22	544,719.	149,081.	14,040.	
23 Adjusted basis. Subtract line 22 from line 21	23	142,573.	145,430.	21,912.	
24 Total gain. Subtract line 23 from line 20	24	118,427.	15,070.	4,764.	
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	544,719.	149,081.	14,040.	
b Enter the smaller of line 24 or 25a	25b	118,427.	15,070.	4,764.	
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

See instructions.

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See instructions for where to report	35		

Form **8594** (Rev. July 1998)
Department of the Treasury
Internal Revenue Service

Asset Acquisition Statement Under Section 1060

▶ Attach to your Federal income tax return.

Attachment Sequence No. 61

Name as shown on return

HOKE CONCRETE & SUPPLY, LLC

Identification number as shown on return

56-2136387

Check the box that identifies you: ☐ Buyer ☒ Seller

Part I General Information - To be completed by all filers.

1 Name of other party to the transaction

CENTRAL CONCRETE CO

Other party's identification number

56-1099304

Address (number, street, and room or suite no.)

P O BOX 131

City or town, state, and ZIP code

BURLINGTON, NC 27216-0131

2 Date of sale

08/31/99

3 Total sales price

10,623,348.

Part II Assets Transferred - To be completed by all filers of an original statement.

4 Assets	Aggregate Fair Market Value (As Stated Amount for Class I)	Allocation of Sales Price
Class I	$	$
Class II	$	$
Class III	$ 7,421,876.	$ 7,421,876.
Class IV and V	$ 3,201,472.	$ 3,201,472.
Total	$ 10,623,348.	$ 10,623,348.

5 Did the buyer and seller provide for an allocation of the sales price or the sales contract or in another written document signed by both parties? ☒ Yes ☐ No

If "Yes," are the aggregate fair market values listed for each of asset Classes I, II, III, IV and V the amounts agreed upon in your sales contract or in a separate written document? ☒ Yes ☐ No

6 In connection with the purchase of the group of assets, did the buyer also purchase a license or a covenant not to compete, or enter into a lease agreement, employment contract, management contract, or similar arrangement with the seller (or managers, directors, owners, or employees of the seller)? ☐ Yes ☒ No

If "Yes," specify (a) the type of agreement, and (b) the maximum amount of consideration (not including interest) paid or to be paid under the agreement. See the instructions for line 6.

LHA For Paperwork Reduction Act Notice, see instructions. Form 8594 (Rev. 7-98)

10

12210331 767285 1233 1999.05200 HOKE CONCRETE & SUPPLY, LLC 1233 1

HOME CONCRETE & SUPPLY, LLC 56-2136387

Form 8594 (Rev. / -98) Page 2

Part III Supplemental Statement - To be completed only if amending an original statement or previously filed supplemental statement because of an increase or decrease in consideration.

7 Assets	Allocation of Sales Price as Previously Reported	Increase or (Decrease)	Reallocated Allocation of Sales Price
Class I	$	$	$
Class II	$	$	$
Class III	$	$	$
Class IV and V	$	$	$
Total	$		$

8 Reason(s) for increase or decrease. Attach additional sheets if more space is needed.

9 Tax year and tax return form number with which the original Form 8594 and any supplemental statement were filed.

HOKE CONCRETE & SUPPLY, LLC 56-2136387

FORM 1065	OTHER INCOME	STATEMENT 1
DESCRIPTION		AMOUNT
MISCELLANEOUS		46,812.
IRSA REBATES		45,054.
TOTAL TO FORM 1065, LINE 7		91,866.

FORM 1065	TAX EXPENSE	STATEMENT 2
DESCRIPTION		AMOUNT
FICA TAX		39,694.
FUTA TAX		311.
SUTA TAX		190.
PROPERTY TAXES		17,164.
SALES TAX		19,394.
TOTAL TO FORM 1065, LINE 16		76,753.

FORM 1065	OTHER DEDUCTIONS	STATEMENT 3
DESCRIPTION		AMOUNT
UTILITIES		7,952.
TELEPHONE		4,612.
INSURANCE		24,659.
OFFICE EXPENSE		13,196.
TRAVEL		300.
TRUCK EXPENSE		74,847.
LEGAL & PROFESSIONAL		13,467.
CONTRACT LABOR		3,150.
COLLECTION FEES		100.
PENSION PLAN ADMINISTRATION		624.
SUPPLIES		1,956.
CASH OVER & SHORT		2,758.
DUES & SUBSCRIPTIONS		632.
REFUNDS		4,452.
CONCRETE WARRENTY EXPENSE		781.
DISCOUNTS		48.
RETURNED CHECKS		2,096.
UNIFORMS		2,306.
CONCRETE TESTING EXPENSE		74.
MISSCELLANEOUS		47.
DIRECTOR FEES		6,750.

HOME CONCRETE & SUPPLY, LLC	56-2136387
SERVICE CHARGES	6,153.
ADVERTISING	6,138.
MEALS AND ENTERTAINMENT	345.
TOTAL TO FORM 1065, LINE 20	177,443.

SCHEDULE K — INTEREST INCOME — STATEMENT 4

DESCRIPTION	U.S. BONDS	OTHER
BANKS		16,819.
U S TREASURY NOTES	<114,206.>	
TOTAL TO SCHEDULE K, LINE 4A	<114,206.>	16,819.

SCHEDULE K — NONDEDUCTIBLE EXPENSE — STATEMENT 5

DESCRIPTION	AMOUNT
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	345.
TOTAL TO SCHEDULE K, LINE 21	345.

HOME CONCRETE & SUPPLY, LLC 56-2136387

SCHEDULE K ADJUSTED GAIN OR LOSS STATEMENT 6

	TOTAL AMOUNT	25%/28% RATE AMOUNT
ALLOCABLE TO SHORT-TERM CAPITAL GAIN OR LOSS		
ALLOCABLE TO LONG-TERM CAPITAL GAIN OR LOSS		
ALLOCABLE TO SECTION 1231 GAIN OR LOSS	<637,849.>	
ALLOCABLE TO ORDINARY GAIN OR LOSS		
ALLOCABLE TO UNRECAPTURED SECTION 1250 GAIN		
TOTAL TO SCHEDULE K, LINE 16B	<637,849.>	

SCHEDULE M-2 DISTRIBUTIONS STATEMENT 7

DESCRIPTION	AMOUNT
TRANSFERRED CAPITAL	5,925,453.
CASH WITHDRAWALS	8,693,414.
TOTAL TO SCHEDULE M-2, LINE 6A	14,618,867.

SCHEDULE L OTHER CURRENT ASSETS STATEMENT 8

DESCRIPTION	BEGINNING OF TAX YEAR	END OF TAX YEAR
SALE ESCROW RECEIVABLE		1,000,000.
TOTAL TO SCHEDULE L, LINE 6		1,000,000.

SCHEDULE L OTHER CURRENT LIABILITIES STATEMENT 9

DESCRIPTION	BEGINNING OF TAX YEAR	END OF TAX YEAR
INTERCOMPANY PAYABLE		258,138.
DISTRIBUTIONS PAYABLE		1,476.
TOTAL TO SCHEDULE L, LINE 17		259,614.

DOJ-018175

HOME CONCRETE & SUPPLY, LLC 56-2136387

FORM 1065 PARTNERS' CAPITAL ACCOUNT SUMMARY STATEMENT 10

PARTNER NUMBER	BEGINNING CAPITAL	CAPITAL CONTRIBUTED	SCHEDULE M-2 [illegible]	WITH- [illegible]	ENDING CAPITAL
1	0.	10,272,847.			696,289.
2	0.	70,785.	→ Ø		626.
3	0.	1,171,957.			10,314.
4	0.	2,450,892.			21,565.
5	0.	2,450,892.			21,565.
TOTAL	0.	16,417,373.			750,359.

HOME CONCRETE & SUPPLY, LLC 56-2136387

SCHEDULE M-1 EXPENSES RECORDED ON BOOKS NOT DEDUCTED IN RETURN STATEMENT 11

DESCRIPTION	AMOUNT
OTHER MISCELLANEOUS EXPENSES	2,474.
TOTAL TO SCHEDULE M-1, LINE 4	2,474.

FORM 1065 CALCULATION OF PARTNERS' EFFECTIVE RATIOS STATEMENT 12

PARTNER NUMBER AND NAME

	TIME PERIOD FROM - THROUGH	DAYS	PERCENTAGE DURING PERIOD	EFFECT. RATIO PER PERIOD	TOTAL EFFECT. RATIO
1	HOME OIL & COAL COMPANY, INC				
	04/15/99 - 06/13/99	60	.982700000	.225908046	
	06/14/99 - 12/31/99	201	.999827000	.769981713	.995889759
2	ROBERT L PIERCE				
	04/15/99 - 06/13/99	60	.000200000	.000045977	
	06/14/99 - 12/31/99	201	.000002000	.000001540	.000047517
3	STEPHEN A CHANDER				
	04/15/99 - 06/13/99	60	.003300000	.000758621	
	06/14/99 - 12/31/99	201	.000033000	.000025414	.000784035
4	THE 1999 ROBERT L PIERCE GRANTOR TRU				
	04/15/99 - 06/13/99	60	.006900000	.001586207	
	06/14/99 - 12/31/99	201	.000069000	.000053138	.001639345
5	THE 1999 ROBERT L PIERCE GRANTOR TRUS				
	04/15/99 - 06/13/99	60	.006900000	.001586207	
	06/14/99 - 12/31/99	201	.000069000	.000053137	.001639344

SCHEDULE M-2 CONTRIBUTIONS STATEMENT 13

DESCRIPTION	AMOUNT
TRANSFERRED CAPITAL	5,925,453.
CONTRIBUTIONS TO CAPITAL	10,491,920.
TOTAL TO SCHEDULE M-2, LINE 2	16,417,373.

Case 7:06-cv-00181-FL Document 26-2 Filed 04/19/07 Page 1 of 3
DOJ-018177

Home Concrete & Supply, LLC (the "partnership")
EIN 56-2136387
A STATEMENT ATTACHED TO AND MADE PART OF FORM 1065
U.S. PARTNERSHIP RETURN OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 1999

ELECTION TO ADJUST BASIS OF PARTNERSHIP PROPERTY

The partnership hereby elects, under the provisions of Sec. 754 to adjusts the basis of partnership property in the manner as approved by Sec. 734(b) and Sec. 743(b). The following information is submitted in accordance with Treas. Reg. 7.754-1(b)(1).

Transferors:

1. Robert L. Pierce SSN [redacted]
   [redacted]
   Salisbury, NC [redacted]

2. Stephen R. Chandler SSN [redacted]
   [redacted]
   Salisbury, NC [redacted]

3. The 1999 Robert L Pierce Grantor Trust A FBO Julie M Pierce EIN 58-6388882
   310 Bethel Drive
   Salisbury, NC 28144

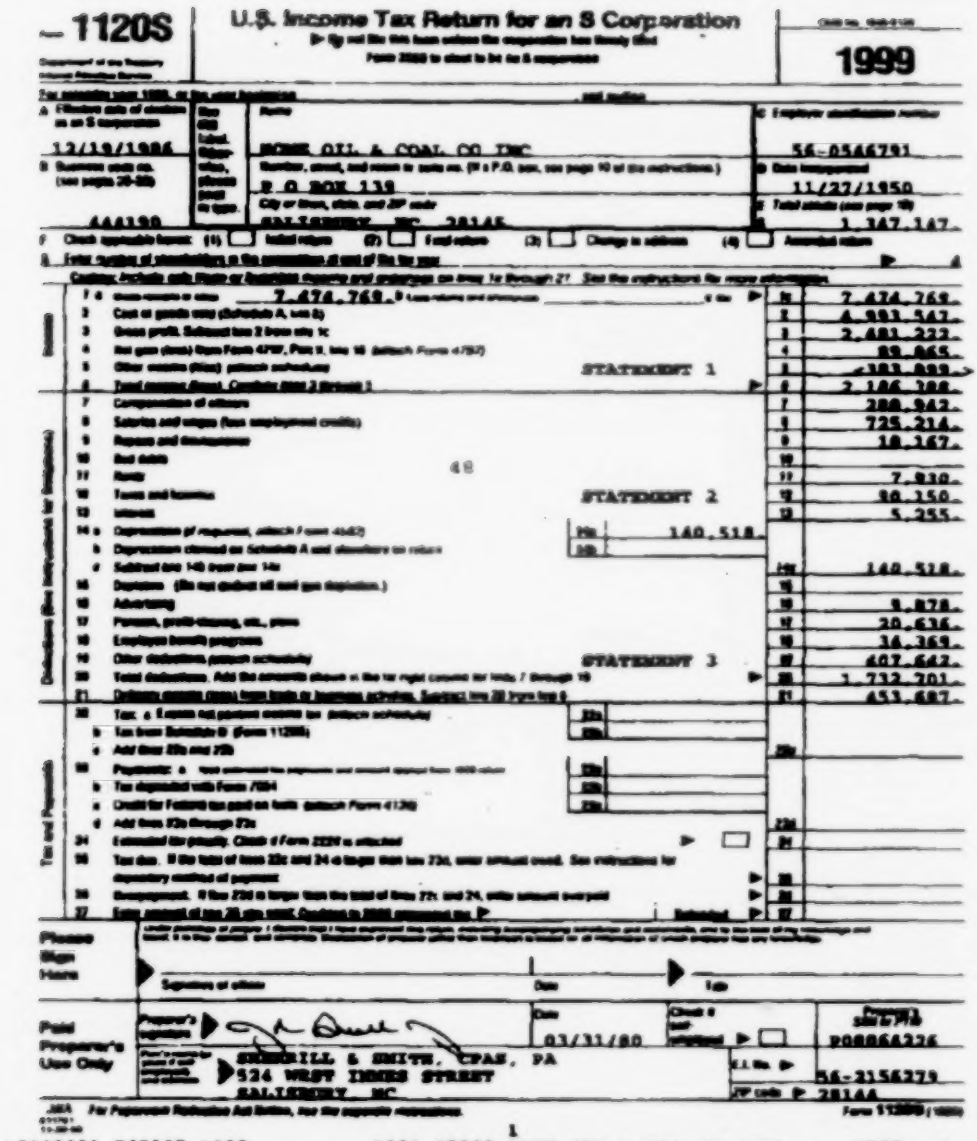
4. The 1999 Robert L Pierce Grantor Trust B FBO Robert C.Pierce EIN 58-6388883
   310 Bethel Drive
   Salisbury, NC 28144

Robert L. Pierce
General Partner

[redacted]

[redacted]

[redacted]



Form 1120S — U.S. Income Tax Return for an S Corporation — 1999

For calendar year 1999, or tax year beginning , and ending

A Effective date of election as an S corporation: 12/19/1986
B Business code no. (see pages 20-22): 444190
C Name: MOORE OIL & COAL CO INC
Number, street, and room or suite no. (If a P.O. box, see page 10 of the instructions.): P O BOX 139
City or town, state, and ZIP code: SALISBURY NC 28145
D Employer identification number: 56-0566791
E Date incorporated: 11/27/1950
F Total assets (see page 10): $ 1,347,167.
G Check applicable boxes: (1) Initial return (2) Final return (3) Change in address (4) Amended return
H Enter number of shareholders in the corporation at end of the tax year

Caution: Include only trade or business income and expenses on lines 1a through 21. See the instructions for more information.

Income	1a Gross receipts or sales	7,474,769.	1c	7,474,769.
	2 Cost of goods sold (Schedule A, line 8)		2	4,993,547.
	3 Gross profit. Subtract line 2 from line 1c		3	2,481,222.
	4 Net gain (loss) from Form 4797, Part II, line 18 (attach Form 4797)		4	89,865.
	5 Other income (loss) (attach schedule) STATEMENT 1		5	-383,899.
	6 Total income (loss). Combine lines 3 through 5		6	2,186,188.
Deductions (See instructions for limitations)	7 Compensation of officers		7	288,942.
	8 Salaries and wages (less employment credits)		8	725,214.
	9 Repairs and maintenance		9	18,167.
	10 Bad debts		10	
	11 Rents		11	7,930.
	12 Taxes and licenses STATEMENT 2		12	80,150.
	13 Interest		13	5,255.
	14a Depreciation (if required, attach Form 4562)	14a 140,518.		
	b Depreciation claimed on Schedule A and elsewhere on return	14b		
	c Subtract line 14b from line 14a		14c	140,518.
	15 Depletion (Do not deduct oil and gas depletion.)		15	
	16 Advertising		16	9,878.
	17 Pension, profit-sharing, etc., plans		17	20,636.
	18 Employee benefit programs		18	14,369.
	19 Other deductions (attach schedule) STATEMENT 3		19	407,642.
	20 Total deductions. Add the amounts shown in the far right column for lines 7 through 19		20	1,732,701.
	21 Ordinary income (loss) from trade or business activities. Subtract line 20 from line 6		21	453,487.
Tax and Payments	22a Tax. a If required, attach Form 8611 (see instructions)	22a		
	b Tax from Schedule D (Form 1120S)	22b		
	c Add lines 22a and 22b		22c	
	23a 1999 estimated tax payments and amount applied from 1998 return	23a		
	b Tax deposited with Form 7004	23b		
	c Credit for Federal tax paid on fuels (attach Form 4136)	23c		
	d Add lines 23a through 23c		23d	
	24 Estimated tax penalty. Check if Form 2220 is attached		24	
	25 Tax due. If the total of lines 22c and 24 is larger than line 23d, enter amount owed. See instructions for depository method of payment		25	
	26 Overpayment. If line 23d is larger than the total of lines 22c and 24, enter amount overpaid		26	
	27 Enter amount of line 26 you want: Credited to 2000 estimated tax	Refunded	27	

Please Sign Here: Signature of officer — Date — Title

Paid Preparer's Use Only: Preparer's signature — Date 03/31/00 — Check if self-employed — Preparer's SSN or PTIN P00866226
Firm's name (or yours if self-employed), address, and ZIP code: SHERRILL & SMITH, CPAS, PA, 524 WEST INNES STREET, SALISBURY NC — EIN 56-2156279 — ZIP code 28144

For Paperwork Reduction Act Notice, see the separate instructions. Form 1120S (1999)

15190331 767285 1233 1999.05200 MOORE OIL & COAL CO INC 1233 1

Form 7004 (Rev. July 1998)
Department of the Treasury
Internal Revenue Service

Application for Automatic Extension of Time To File Corporation Income Tax Return

OMB No. 1545-0233

Name of corporation

HOWE OIL & COAL CO INC

Employer identification number

56-0546791

Number, street, and room or suite no. (If a P.O. box or outside the United States, see instructions.)

P O BOX 139

City or town, state, and ZIP code

SALISBURY, NC 28145

Check type of return to be filed:

- ☐ Form 1120
- ☒ Form 1120-A
- ☐ Form 1120-F
- ☐ Form 1120-FSC
- ☐ Form 1120-H
- ☐ Form 1120-L
- ☐ Form 1120-ND
- ☐ Form 1120-PC
- ☐ Form 1120-PCL
- ☐ Form 1120-REIT
- ☐ Form 1120-RIC
- ☒ Form 1120S
- ☐ Form 1120-SF

☐ Form 990-C
☐ Form 990-T ▶ Note. Other 990 filers (i.e., Form 990, 990-EZ, 990-BL, 990-PF, and certain filers of Form 990-T (see instructions)) must use Form 2758 to request an extension of time to file.

Form 1120-F filers: Check here if you do not have an office or place of business in the United States ▶ ☐

1a I request an automatic 6-month (or, for certain foreign corporations, 3-month) extension of time until SEPTEMBER 15, 2000, to file the income tax return of the corporation named above for ▶ ☒ calendar year 1999 or ▶ ☐ tax year beginning _____, _____, and ending _____, _____.

b If this tax year is for less than 12 months, check reason:
☐ Initial return ☐ Final return ☐ Change in accounting period ☐ Consolidated return to be filed

2 If this application also covers subsidiaries to be included in a consolidated return, complete the following.

Name and address of each member of the affiliated group	Employer identification number	Tax period

3 Tentative tax 3 0.

4 Credits:
a Overpayment credited from prior year 4a
b Estimated tax payments for the tax year 4b
c Less refund for the tax year applied for on Form 4466 4c ( ) Bal ▶ 4d
e Credit for tax paid on undistributed capital gains (Form 2439) 4e
f Credit for Federal tax on fuels (Form 4136) 4f

5 Total. Add lines 4d through 4f 5 0.

6 Balance due. Subtract line 5 from line 3. Deposit this amount electronically or with a Federal Tax Deposit (FTD) Coupon 6 0.

Signature. Under penalties of perjury, I declare that I have been authorized by the above named corporation to make this application, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than officer or agent) is based on all information of which preparer has any knowledge.

CPA
Signature of officer or agent Title 3-14-00 Date

For Paperwork Reduction Act Notice, see instructions. Form 7004 (Rev. 7-98)

10510314 767285 1232 1999.04200 HOWE OIL & COAL CO INC 1232 1

Form 1120 (1998) MOHER OIL & COAL CO INC 56-0546791 Page 2

Schedule A Cost of Goods Sold

1	Inventory at beginning of year	1	854,263.
2	Purchases	2	4,139,284.
3	Cost of labor	3	
4	Additional section 263A costs (attach schedule)	4	
5	Other costs (attach schedule)	5	
6	Total. Add lines 1 through 5	6	4,993,547.
7	Inventory at end of year	7	
8	Cost of goods sold. Subtract line 7 from line 6. Enter here and on page 1, line 2	8	4,993,547.

9a Check all methods used for valuing closing inventory:
- (i) ☐ Cost as described in Regulations section 1.471-3
- (ii) ☒ Lower of cost or market as described in Regulations section 1.471-4
- (iii) ☐ Other (specify method used and attach explanation) ▶

b Check if there was a writedown of "subnormal" goods as described in Regulations section 1.471-2(c) ▶ ☐

c Check if the LIFO inventory method was adopted this tax year for any goods (if checked, attach Form 970) ▶ ☐

d If the LIFO inventory method was used for this tax year, enter percentage (or amounts) of closing inventory computed under LIFO 9d

e Do the rules of section 263A (for property produced or acquired for resale) apply to the corporation? ☒ Yes ☐ No

f Was there any change in determining quantities, cost, or valuations between opening and closing inventory? ☐ Yes ☒ No

If "Yes," attach explanation.

Schedule B Other Information

		Yes	No
1	Check method of accounting: (a) ☐ Cash (b) ☒ Accrual (c) ☐ Other (specify) ▶		
2	Refer to the list on pages 26 through 28 of the instructions and state the corporation's principal: (a) Business activity ▶ RETAIL (b) Product or service ▶ OIL PRODUCTS/CONCRETE		
3	Did the corporation at the end of the tax year own, directly or indirectly, 50% or more of the voting stock of a domestic corporation? (For rules of attribution, see section 267(c).) If "Yes," attach a schedule showing: (a) name, address, and employer identification number and (b) percentage owned		X
4	Was the corporation a member of a controlled group subject to the provisions of section 1561?		X
5	At any time during calendar year 1998, did the corporation have an interest in or a signature or other authority over a financial account in a foreign country (such as a bank account, securities account, or other financial account)? (See page 15 of the instructions for exceptions and filing requirements for Form TD F 90-22.1.) If "Yes," enter the name of the foreign country ▶		X
6	During the tax year, did the corporation receive a distribution from, or was it the grantor of, or transferor to, a foreign trust? If "Yes," the corporation may have to file Form 3520. See page 15 of the instructions		X
7	Check this box if the corporation has filed or is required to file Form 8264, Application for Registration of a Tax Shelter ▶ ☐		
8	Check this box if the corporation issued publicly offered debt instruments with original issue discount ▶ ☐ If so, the corporation may have to file Form 8281, Information Return for Publicly Offered Original Issue Discount Instruments.		
9	If the corporation: (a) filed its election to be an S corporation after 1986, (b) was a C corporation before it elected to be an S corporation or the corporation acquired an asset with a basis determined by reference to its basis (or the basis of any other property) in the hands of a C corporation, and (c) has net unrealized built-in gain (defined in section 1374(d)(1)) in excess of the net recognized built-in gain from prior years, enter the net unrealized built-in gain reduced by net recognized built-in gain from prior years ▶ $		
10	Check this box if the corporation had accumulated earnings and profits at the close of the tax year ▶ ☐		

Form 1120S (1998)

15190331 767285 1232 1999.05200 MOHER OIL & COAL CO INC 1232___1

Form 1120S (1999) HORSE OIL & COAL CO INC 56-0546791 Page 3

Schedule K Shareholders' Shares of Income, Credits, Deductions, etc.

			(a) Total amount
Income (Loss)	1 Ordinary income (loss) from trade or business activities (page 1, line 21)	1	453,687.
	2 Net income (loss) from rental real estate activities (attach Form 8825)	2	
	3a Gross income from other rental activities — 3a		
	b Expenses from other rental activities (attach schedule) — 3b		
	c Net income (loss) from other rental activities. Subtract line 3b from line 3a	3c	
	4 Portfolio income (loss):		
	a Interest income STATEMENT 5	4a	<53,663.>
	b Ordinary dividends	4b	
	c Royalty income	4c	
	d Net short-term capital gain (loss) (attach Schedule D (Form 1120S))	4d	112,896.
	e Net long-term capital gain (loss) (attach Schedule D (Form 1120S)):		
	(1) 28% rate gain (loss) ▶ _____ (2) Total for year ▶	4e(2)	<161,879.>
	f Other portfolio income (loss) (attach schedule)	4f	
	5 Net section 1231 gain (loss) (other than due to casualty or theft) (attach Form 4797) STATEMENT 6	5	<110,362.>
	6 Other income (loss) (attach schedule)	6	
Deductions	7 Charitable contributions (attach schedule) STATEMENT 7	7	2,169.
	8 Section 179 expense deduction (attach Form 4562)	8	
	9 Deductions related to portfolio income (loss) (attach schedule)	9	
	10 Other deductions (attach schedule)	10	
Investment Interest	11a Interest expense on investment debts	11a	
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	11b(1)	<53,663.>
	(2) Investment expenses included on line 9 above	11b(2)	
Credits	12a Credit for alcohol used as a fuel (attach Form 6478)	12a	
	b Low-income housing credit:		
	(1) From partnerships to which section 42(j)(5) applies for property placed in service before 1990	12b(1)	
	(2) Other than on line 12b(1) for property placed in service before 1990	12b(2)	
	(3) From partnerships to which section 42(j)(5) applies for property placed in service after 1989	12b(3)	
	(4) Other than on line 12b(3) for property placed in service after 1989	12b(4)	
	c Qualified rehabilitation expenditures related to rental real estate activities (attach Form 3468)	12c	
	d Credits (other than credits shown on lines 12b and 12c) related to rental real estate activities	12d	
	e Credits related to other rental activities	12e	
	13 Other credits	13	
Adjustments and Tax Preference Items	14a Depreciation adjustment on property placed in service after 1986	14a	7,587.
	b Adjusted gain or loss STATEMENT 8	14b	<635,227.>
	c Depletion (other than oil and gas)	14c	
	d (1) Gross income from oil, gas, or geothermal properties	14d(1)	
	(2) Deductions allocable to oil, gas, or geothermal properties	14d(2)	
	e Other adjustments and tax preference items (attach schedule)	14e	
Foreign Taxes	15a Type of income ▶ _____		
	b Name of foreign country or U.S. possession ▶ _____		
	c Total gross income from sources outside the United States (attach schedule)	15c	
	d Total applicable deductions and losses (attach schedule)	15d	
	e Total foreign taxes (check one): ▶ ☐ Paid ☐ Accrued	15e	
	f Reduction in taxes available for credit (attach schedule)	15f	
	g Other foreign tax information (attach schedule)	15g	
Other	16 Section 59(e)(2) expenditures: a Type ▶ _____		
	b Amount	16b	
	17 Tax-exempt interest income	17	
	18 Other tax-exempt income	18	
	19 Nondeductible expenses STATEMENT 9	19	1,851.
	20 Total property distributions (including cash) other than dividends reported on line 22 below	20	9,760,145.
	21 Other items and amounts required to be reported separately to shareholders (attach schedule) STATEMENT 10		
	22 Total dividend distributions paid from accumulated earnings and profits	22	
	23 Income (loss). (Required only if Schedule M-1 must be completed.) Combine lines 1 through 6 in column (a). From the result, subtract the sum of lines 7 through 11a, 12e, and 13	23	239,110.

Form 1120S (1999)

19198331 767285 1232 1999.05200 HORSE OIL & COAL CO INC 1232___1

DOJ-018956

Form 1120S (1999) BOWER OIL & COAL CO INC 56-0546791 Page 4

Schedule L Balance Sheets

Assets	Beginning of tax year (a)	(b)	End of tax year (c)	(d)
1 Cash		1,699,219.		192,720.
2a Trade notes and accounts receivable	1,911,798.			
b Less allowance for bad debts	12,158.	1,901,640.		
3 Inventories		790,941.		
4 U.S. Government obligations				
5 Tax-exempt securities				
6 Other current assets STMT 13		156,612.		258,138.
7 Loans to shareholders				
8 Mortgage and real estate loans				
9 Other investments STMT 14				696,289.
10a Buildings and other depreciable assets	4,904,625.			
b Less accumulated depreciation	3,332,310.	1,572,315.		
11a Depletable assets				
b Less accumulated depletion				
12 Land (net of any amortization)		110,565.		
13a Intangible assets (amortizable only)				
b Less accumulated amortization				
14 Other assets				
15 Total assets		6,251,274.		1,347,147.
Liabilities and Shareholders' Equity				
16 Accounts payable		904,532.		
17 Mortgages, notes, bonds payable in less than 1 year		67,923.		24,185.
18 Other current liabilities STMT 15		170,144.		
19 Loans from shareholders				
20 Mortgages, notes, bonds payable in 1 year or more		24,186.		
21 Other liabilities				
22 Capital stock		5,300.		5,300.
23 Additional paid-in capital				
24 Retained earnings STMT 19		4,879,189.		1,317,662.
25 Adjustments to shareholders' equity				
26 Less cost of treasury stock		( )		( )
27 Total liabilities and shareholders' equity		6,251,274.		1,347,147.

Schedule M-1 Reconciliation of Income (Loss) per Books With Income (Loss) per Return (You are not required to complete this schedule if the total assets on line 15, column (d), of Schedule L are less than $25,000.)

1 Net income (loss) per books	273,165.	6 Income recorded on books this year not included on Schedule K, lines 1 through 6 (itemize): a Tax-exempt interest $	
2 Income included on Schedule K, lines 1 through 6, not recorded on books this year (itemize)			
STMT 16	13,307.		
3 Expenses recorded on books this year not included on Schedule K, lines 1 through 11a, 15e, and 16b (itemize): a Depreciation $		7 Deductions included on Schedule K, lines 1 through 11a, 15e, and 16b, not charged against book income this year (itemize): a Depreciation $	
b Travel and entertainment $ 1,043.		STMT 18 63,320.	63,320.
STMT 17 15,115.	16,158.	8 Add lines 5 and 6	63,320.
4 Add lines 1 through 3	102,638.	9 Income (loss) (Schedule K, line 23). Line 4 less line 7	219,310.

Schedule M-2 Analysis of Accumulated Adjustments Account, Other Adjustments Account, and Shareholders' Undistributed Taxable Income Previously Taxed

	(a) Accumulated adjustments account	(b) Other adjustments account	(c) Shareholders' undistributed taxable income previously taxed
1 Balance at beginning of tax year	1,507,936.		
2 Ordinary income from page 1, line 21	451,687.		
3 Other additions STMT 11	6,848,886.		
4 Loss from page 1, line 21	( )		
5 Other reductions STMT 12	(103,875.)	( )	
6 Combine lines 1 through 5	9,706,554.		
7 Distributions other than dividend distributions	9,706,554.		
8 Balance at end of tax year. Subtract line 7 from line 6	0.		

SCHEDULE D (Form 1120) — Capital Gains and Losses and Built-in Gains — 1999

▶ Attach to Form 1120.

Name: BOWE OIL & COAL CO INC

Employer identification number: 56-0546791

Part I Short-Term Capital Gains and Losses - Assets Held One Year or Less

(a) Description of property	(b) Date acquired	(c) Date sold	(d) Sales price	(e) Cost or other basis	(f) Gain or (loss)
1 PASSTHROUGH FROM BOWE CONCRETE & SUPPLY LLC					112,896.
2 Short-term capital gain from installment sales from Form 6252, line 26 or 37				2	
3 Short-term capital gain or (loss) from like-kind exchanges from Form 8824				3	
4 Combine lines 1 through 3 in column (f) and enter here				4	112,896.
5 Tax on short-term capital gain included on line 29 below				5	( )
6 Net short-term capital gain or (loss). Combine lines 4 and 5. Enter here and on Page 1, line 8, column (a)				6	112,896.

Part II Long-Term Capital Gains and Losses - Assets Held More Than One Year

(a) Description of property	(b) Date acquired	(c) Date sold	(d) Sales price	(e) Cost or other basis	(f) Gain or (loss)	(g) 28% rate gain or (loss) *
7 SALE OF LAND	10/24/97	03/19/99	1,981.	1,525.	456.	
8 PASSTHROUGH FROM BOWE CONCRETE & SUPPLY LLC					<161,537.>	0.
9 Long-term capital gain from installment sales from Form 6252, line 26 or 37				9		
10 Long-term capital gain or (loss) from like-kind exchanges from Form 8824				10		
11 Combine lines 7 through 10 in column (f) and enter here				11	<161,081.>	
12 Tax on long-term capital gain included on lines 34 and 37 below				12	( )	( )
13 Combine lines 7 through 11 in column (g). Enter here and on Form 1120, Schedule K, line 4a(1) or 5				13		
14 Net long-term capital gain or (loss). Combine lines 10 and 11 in column (f). Enter here and on Form 1120, Schedule K, line 4a(2) or 5				14	<161,081.>	

* 28% rate gain or (loss) includes all "collectibles gains and losses" (as defined in the instructions).

Part III Capital Gains Tax. (See instructions before completing this part.)

15 Enter smaller of line 6 or line 14	15	
16 Net long-term capital gain or (loss). Combine lines 14 and 15	16	
Note: If the corporation is liable for the excess net passive income tax (Form 1120S, page 1, line 22a) or the built-in gains tax (Part IV below), see the line 16 instructions before completing line 16.		
17 Net capital gain. Enter excess of net long-term capital gain (line 16) over net short-term capital loss (line 6)	17	
18 Statutory maximum	18	$25,000
19 Subtract line 17 from line 16	19	
20 Enter 34% of line 16	20	
21 Tentative income (attach computation schedule)	21	
22 Enter tax on line 21 amount (attach computation) ▶	22	
23 Net capital gain from substituted basis property ▶ , computation schedule)	23	
24 Enter 35% of line 23	24	
25 Tax. Enter the smallest of line 19, 21, or 24 here and on Form 1120, page 1, line 23b	25	

Part IV Built-in Gains Tax. (See instructions before completing this part.)

26 Excess of recognized built-in gains over recognized built-in losses (attach computation schedule)	26	
27 Taxable income (attach computation schedule)	27	
28 Net recognized built-in gain. Enter smaller of line 26, line 26b, or line 9 of Schedule B	28	
29 Section 1374(b)(2) deduction	29	
30 Subtract line 29 from line 27. If zero or less, enter -0- here and on line 32.	30	
31 Enter 35% of line 30	31	
32 Business credit and minimum tax credit carryforwards under section 1374(b)(2) from C corporation years	32	
33 Tax. Subtract line 31 from line 28 (if zero or less, enter -0-). Enter here and on Form 1120, page 1, line 23b	33	

JSA — For Paperwork Reduction Act Notice, see the instructions for Form 1120S. — Schedule D (Form 1120S) 1999

5

15190331 767285 1232 — 1999.05200 BOWE OIL & COAL CO INC — 1232___1

SCHEDULE K-1 (Form 1120S)

Shareholder's Share of Income, Credits, Deductions, etc.

▶ See separate instructions.

For calendar year 1999 or tax year beginning ____ and ending ____

1999

Shareholder's identifying number ▶ [redacted]

Shareholder's name, address, and ZIP code

ROBERT L PIERCE
[redacted]
[redacted]

Corporation's identifying number ▶ 56-0546791

Corporation's name, address, and ZIP code

HOME OIL & COAL CO INC
P O BOX 139
[redacted]

A Shareholder's percentage of stock ownership for tax year (see instructions for Schedule K-1) ▶ 26.117917%

B Internal Revenue Service Center where corporation filed its return ▶ MEMPHIS, TN

C Tax shelter registration number (see instructions for Schedule K-1) ▶

D Check applicable boxes: (1) ☐ Final K-1 (2) ☐ Amended K-1

	(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on:
Income (Loss)	1 Ordinary income (loss) from trade or business activities	1	119,492.	See pages 4 and 5 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	2 Net income (loss) from rental real estate activities	2		
	3 Net income (loss) from other rental activities	3		
	4 Portfolio income (loss):			
	a Interest SEE STATEMENT	4a	<14,134.	Sch. B, Part I, line 1
	b Ordinary dividends	4b		Sch. B, Part II, line 5
	c Royalties	4c		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	4d	29,736.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss):			
	(1) 28% rate gain (loss)	4e(1)		Sch. D, line 12, col. (g)
	(2) Total for year	4e(2)	<42,425.	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)	4f		Enter on applicable line of your return.
	5 Net section 1231 gain (loss) (other than due to casualty or theft) STMT	5	<29,067.	See Shareholder's Instructions for Schedule K-1 (Form 1120S)
	6 Other income (loss) (attach schedule)	6		Enter on applicable line of your return.
Deductions	7 Charitable contributions (attach schedule) SEE STATEMENT	7	571.	Sch. A, line 15 or 16
	8 Section 179 expense deduction	8		See page 6 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	9 Deductions related to portfolio income (loss) (attach schedule)	9		
	10 Other deductions (attach schedule)	10		
Investment Interest	11a Interest expense on investment debts	11a		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	11b(1)	<14,134.	See Shareholder's Instructions for Schedule K-1 (Form 1120S)
	(2) Investment expenses included on line 9 above	11b(2)		
Credits	12a Credit for alcohol used as fuel	12a		Form 6478, line 10
	b Low-income housing credit:			
	(1) From section 42(j)(5) partnerships for property placed in service before 1990	12b(1)		Form 8586, line 5
	(2) Other than on line 12b(1) for property placed in service before 1990	12b(2)		
	(3) From section 42(j)(5) partnerships for property placed in service after 1989	12b(3)		
	(4) Other than on line 12b(3) for property placed in service after 1989	12b(4)		
	c Qualified rehabilitation expenditures related to rental real estate activities	12c		See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	d Credits (other than credits shown on lines 12b and 12c) related to rental real estate activities	12d		
	e Credits related to other rental activities	12e		
	13 Other credits	13		

JSA For Paperwork Reduction Act Notice, see the Instructions for Form 1120S. Schedule K-1 (Form 1120S) 1999

15190331 767285 1232 1999.05300 HOME OIL & COAL CO INC 1232 1

18 SHAREHOLDER NUMBER 1

HOWE OIL & COAL CO INC 56-0546791

	(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on
Adjustments and Tax Preference Items	14 a Depreciation adjustment on property placed in service after 1986	14a	1,977.	See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S) and Instructions for Form 6251
	b Adjusted gain or loss SEE STATEMENT	14b	<167,186.	
	c Depletion (other than oil and gas)	14c		
	d (1) Gross income from oil, gas, or geothermal properties	d(1)		
	(2) Deductions allocable to oil, gas, or geothermal properties	d(2)		
	e Other adjustments and tax preference items (attach schedule)	14e		
Foreign Taxes	15 a Type of income ▶			Form 1116, Check boxes
	b Name of foreign country or U.S. possession ▶			
	c Total gross income from sources outside the United States (attach schedule)	15c		Form 1116, Part I
	d Total applicable deductions and losses (attach schedule)	15d		
	e Total foreign taxes (check one): ▶ ☐ Paid ☐ Accrued	15e		Form 1116, Part II
	f Reduction in taxes available for credit (attach schedule)	15f		Form 1116, Part III
	g Other foreign tax information (attach schedule)	15g		See instructions for Form 1116
Other	16 Section 59(e)(2) expenditures: a Type ▶			See Shareholder's Instructions for Schedule K-1 (Form 1120S)
	b Amount	16b		
	17 Tax-exempt interest income	17		Form 1040, line 8b
	18 Other tax-exempt income	18		
	19 Nondeductible expenses SEE STATEMENT	19	1,015.	See pages 7 and 8 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	20 Property distributions (including cash) other than dividend distributions reported to you on Form 1099-DIV	20	284,056.	
	21 Amount of loan repayments for "Loans From Shareholders"	21		
	22 Recapture of low-income housing credit:			
	a From section 42(j)(5) partnerships	22a		Form 8611, line 8
	b Other than on line 22a	22b		

23 Supplemental information required to be reported separately to each shareholder (attach additional schedules if more space is needed):

QUALIFIES AS SELF EMPLOYED

MEDICAL INSURANCE PREMIUMS 1,462. HEALTH INSURANCE

Supplemental Information

DOJ-018960

HOME OIL & COAL CO INC . 56-0546791

SCHEDULE K-1 INTEREST INCOME

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
U.S. GOVERNMENT INTEREST	<29,956.>	SEE FORM 1040 INSTRUCTIONS
OTHER TAXABLE INTEREST	15,822.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 4A	<14,134.>	

SCHEDULE K-1 SECTION 1231 GAINS(LOSSES)

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
FROM TRADE OR BUSINESS	<29,067.>	SEE FORM 1040 INSTRUCTIONS
TOTAL TO LINE 5	<29,067.>	

SCHEDULE K-1 CHARITABLE CONTRIBUTIONS

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
CHARITABLE CONTRIBUTIONS - 50 % LIMIT	571.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 7	571.	

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<167,306.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 14B	<167,306.>		

Case 7:06-cv-00181-FL Document 27-4 Filed 04/19/07 Page 9 of 32

HOME OIL & COAL CO INC - - 56-0546791

SCHEDULE K-1 NONDEDUCTIBLE EXPENSES

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	275.	SEE FORM 1040 INSTRUCTIONS
NONDEDUCTIBLE EXPENSES FROM PASS THROUGH ENTITIES	740.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 19	1,015.	

DOJ-018962

SCHEDULE K-1 (Form 1120S)

Shareholder's Share of Income, Credits, Deductions, etc.

▶ See separate instructions.

For calendar year 1999 or tax year beginning ____ and ending ____

1999

Shareholder's identifying number ▶ [redacted]

Shareholder's name, address, and ZIP code

STEPHEN R CHANDLER
[redacted]

Corporation's identifying number ▶ 56-0546791

Corporation's name, address, and ZIP code

HOKE OIL & COAL CO INC
P O BOX 139
SALISBURY, NC 28145

A Shareholder's percentage of stock ownership for tax year (see instructions for Schedule K-1) ▶ 18.867925%

B Internal Revenue Service Center where corporation filed its return ▶ MEMPHIS, TN

C Tax shelter registration number (see instructions for Schedule K-1) ▶

D Check applicable boxes: (1) ☐ Final K-1 (2) ☐ Amended K-1

	(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on:
Income (Loss)	1 Ordinary income (loss) from trade or business activities	1	85,601.	See pages 4 and 5 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	2 Net income (loss) from rental real estate activities	2		
	3 Net income (loss) from other rental activities	3		
	4 Portfolio income (loss):			
	a Interest SEE STATEMENT	4a	<10,125.	Sch. B, Part I, line 1
	b Ordinary dividends	4b		Sch. B, Part II, line 5
	c Royalties	4c		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	4d	31,102.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss):			
	(1) 28% rate gain (loss)	4e(1)		Sch. D, line 12, col. (g)
	(2) Total for year	4e(2)	<10,192.	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)	4f		Enter on applicable line of your return.
	5 Net section 1231 gain (loss) (other than due to casualty or theft) STMT	5	<20,823.	See Shareholder's Instructions for Schedule K-1 (Form 1120S)
	6 Other income (loss) (attach schedule)	6		Enter on applicable line of your return.
Deductions	7 Charitable contributions (attach schedule) SEE STATEMENT	7	410.	Sch. A, line 15 or 16
	8 Section 179 expense deduction	8		See page 6 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	9 Deductions related to portfolio income (loss) (attach schedule)	9		
	10 Other deductions (attach schedule)	10		
Investment Interest	11a Interest expense on investment debts	11a		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	b(1)	<10,125.	See Shareholder's Instructions for Schedule K-1 (Form 1120S)
	(2) Investment expenses included on line 9 above	b(2)		
Credits	12a Credit for alcohol used as fuel	12a		Form 6478, line 10
	b Low-income housing credit:			
	(1) From section 42(j)(5) partnerships for property placed in service before 1990	b(1)		Form 8586, line 5
	(2) Other than on line 12b(1) for property placed in service before 1990	b(2)		
	(3) From section 42(j)(5) partnerships for property placed in service after 1989	b(3)		
	(4) Other than on line 12b(1) for property placed in service after 1989	b(4)		
	c Qualified rehabilitation expenditures related to rental real estate activities	12c		See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	d Credits (other than credits shown on lines 12b and 12c) related to rental real estate activities	12d		
	e Credits related to other rental activities	12e		
	13 Other credits	13		

For Paperwork Reduction Act Notice, see the instructions for Form 1120S. Schedule K-1 (Form 1120S) 1999

15190331 767285 1232 1999.05200 HOKE OIL & COAL CO INC 22 SHAREHOLDER NUMBER 2 1232 1

HOBET OIL & COAL CO INC 56-0546791

(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on
14 a Depreciation adjustment on property placed in service after 1986	14a	1,417.	
b Adjusted gain or loss SEE STATEMENT	14b	-119,854.	See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S) and Instructions for Form 6251
c Depletion (other than oil and gas)	14c		
d (1) Gross income from oil, gas, or geothermal properties	14d(1)		
(2) Deductions allocable to oil, gas, or geothermal properties	14d(2)		
e Other adjustments and tax preference items (attach schedule)	14e		
15 a Type of income			Form 1116, Check boxes
b Name of foreign country or U.S. possession			
c Total gross income from sources outside the United States (attach schedule)	15c		Form 1116, Part I
d Total applicable deductions and losses (attach schedule)	15d		
e Total foreign taxes (check one): Paid Accrued	15e		Form 1116, Part II
f Reduction in taxes available for credit (attach schedule)	15f		Form 1116, Part III
g Other foreign tax information (attach schedule)	15g		See instructions for Form 1116
16 Section 59(e)(2) expenditures: a Type			See Shareholder's Instructions for Schedule K-1 (Form 1120S)
b Amount	16b		
17 Tax-exempt interest income	17		Form 1040, line 8b
18 Other tax-exempt income	18		
19 Nondeductible expenses SEE STATEMENT	19	725.	See pages 7 and 8 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
20 Property distributions (including cash) other than dividend distributions reported to you on Form 1099-DIV	20	1,841,531.	
21 Amount of loss requirements for "Losses From Shareholders"	21		
22 Recapture of low-income housing credit:			
a From section 42(j)(5) partnerships	22a		Form 8611, line 8
b Other than on line 22a	22b		

23 Supplemental information required to be reported separately to each shareholder (attach additional schedules if more space is needed):

QUALIFIES AS SELF EMPLOYED

MEDICAL INSURANCE PREMIUMS 1,463. HEALTH INSURANCE

Supplemental Information

HOWE OIL & COAL CO INC 56-0546791

SCHEDULE K-1 INTEREST INCOME

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
U.S. GOVERNMENT INTEREST	<21,460.>	SEE FORM 1040 INSTRUCTIONS
OTHER TAXABLE INTEREST	11,335.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 4A	<10,125.>	

SCHEDULE K-1 SECTION 1231 GAINS(LOSSES)

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
FROM TRADE OR BUSINESS	<20,823.>	SEE FORM 1040 INSTRUCTIONS
TOTAL TO LINE 5	<20,823.>	

SCHEDULE K-1 CHARITABLE CONTRIBUTIONS

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
CHARITABLE CONTRIBUTIONS - 50 % LIMIT	410.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 7	410.	

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<119,854.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 14B	<119,854.>		

DOJ-018985

BOMX OIL & COAL CO INC 56-0546791

SCHEDULE K-1 NONDEDUCTIBLE EXPENSES

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	196.	SEE FORM 1040 INSTRUCTIONS
NONDEDUCTIBLE EXPENSES FROM PASS THROUGH ENTITIES	529.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 19	725.	

DOJ-018966

SCHEDULE K-1 (Form 1120S)

Shareholder's Share of Income, Credits, Deductions, etc.

▶ See separate instructions.

For calendar year 1999 or tax year beginning ____ and ending ____

1999

Shareholder's identifying number ▶ 58-6188592

Shareholder's name, address, and ZIP code

THE 1999 ROBERT L PIERCE GRANTOR TRUST A FBO JULIE M PIERCE
310 BETHEL DRIVE
SALISBURY, NC 28144

Corporation's identifying number ▶ 56-0546791

Corporation's name, address, and ZIP code

HOKE OIL & COAL CO INC
P O BOX 139
SALISBURY, NC 28145

A Shareholder's percentage of stock ownership for tax year (see instructions for Schedule K-1) ▶ 27.197078%

B Internal Revenue Service Center where corporation filed its return ▶ MEMPHIS, TN

C Tax shelter registration number (see instructions for Schedule K-1) ▶

D Check applicable boxes: (1) ☐ Final K-1 (2) ☐ Amended K-1

	(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on:
Income (Loss)	1 Ordinary income (loss) from trade or business activities	1	134,297.	See pages 4 and 5 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	2 Net income (loss) from rental real estate activities	2		
	3 Net income (loss) from other rental activities	3		
	4 Portfolio income (loss):			
	a Interest SEE STATEMENT	4a	<14,702.	Sch. B, Part I, line 1
	b Ordinary dividends	4b		Sch. B, Part II, line 5
	c Royalties	4c		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	4d	30,930.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss):			
	(1) 28% rate gain (loss)	4e(1)		Sch. D, line 12, col. (g)
	(2) Total for year	4e(2)	<44,131.	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)	4f		Enter on applicable line of your return
	5 Net section 1231 gain (loss) (other than due to casualty or theft) STMT	5	<30,236.	See Shareholder's Instructions for Schedule K-1 (Form 1120S)
	6 Other income (loss) (attach schedule)	6		Enter on applicable line of your return
Deductions	7 Charitable contributions (attach schedule) SEE STATEMENT	7	594.	Sch. A, line 15 or 16
	8 Section 179 expense deduction	8		See page 6 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	9 Deductions related to portfolio income (loss) (attach schedule)	9		
	10 Other deductions (attach schedule)	10		
Investment Interest	11a Interest expense on investment debts	11a		Form 4952, line 1
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	b(1)	<14,702.	See Shareholder's Instructions for Schedule K-1 (Form 1120S)
	(2) Investment expenses included on line 9 above	b(2)		
Credits	12a Credit for alcohol used as fuel	12a		Form 6478, line 10
	b Low-income housing credit:			
	(1) From section 42(j)(5) partnerships for property placed in service before 1990	b(1)		
	(2) Other than on line 12b(1) for property placed in service before 1990	b(2)		
	(3) From section 42(j)(5) partnerships for property placed in service after 1989	b(3)		Form 8586, line 5
	(4) Other than on line 12b(3) for property placed in service after 1989	b(4)		
	c Qualified rehabilitation expenditures related to rental real estate activities	12c		
	d Credits (other than credits shown on lines 12b and 12c) related to rental real estate activities	12d		See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S)
	e Credits related to other rental activities	12e		
	13 Other credits	13		

AWA For Paperwork Reduction Act Notice, see the Instructions for Form 1120S. Schedule K-1 (Form 1120S) 1999

HOBE OIL & COAL CO INC 56-0566791

Adjustments and Tax Preference Items	14 a	Depreciation adjustment on property placed in service after 1986	14a	2,056.
	b	Adjusted gain or loss SEE STATEMENT	14b	<174,033.
	c	Depletion (other than oil and gas)	14c	
	d	(1) Gross income from oil, gas, or geothermal properties	d(1)	
		(2) Deductions allocable to oil, gas, or geothermal properties	d(2)	
	e	Other adjustments and tax preference items (attach schedule)	14e	
Foreign Taxes	15 a	Type of income ▶		
	b	Name of foreign country or U.S. possession ▶		
	c	Total gross income from sources outside the United States (attach schedule)	15c	
	d	Total applicable deductions and losses (attach schedule)	15d	
	e	Total foreign taxes (check one): ▶ ☐ Paid ☐ Accrued	15e	
	f	Reduction in taxes available for credit (attach schedule)	15f	
	g	Other foreign tax information (attach schedule)	15g	
Other	16	Section 59(e)(2) expenditures: a Type ▶		
	b	Amount	16b	
	17	Tax-exempt interest income	17	
	18	Other tax-exempt income	18	
	19	Nondeductible expenses SEE STATEMENT	19	1,056.
	20	Property distributions (excluding cash) other than dividend distributions reported to you on Form 1099-DIV	20	1,817,279.
	21	Amount of loss recapture for "Loans From Shareholders"	21	
	22	Recapture of low-income housing credit:		
	a	From section 42(j)(5) partnerships	22a	
	b	Other than on line 22a	22b	
Supplemental Information	23	Supplemental information required to be reported separately to each shareholder (attach additional schedules if more space is needed):		

15190331 767285 1232 1993.05200 HOBE OIL & COAL CO INC SHAREHOLDER NUMBER 3 1232 1

HOWE OIL & COAL CO INC 56-0546791

SCHEDULE K-1 INTEREST INCOME

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
U.S. GOVERNMENT INTEREST	<31,160.>	SEE FORM 1040 INSTRUCTIONS
OTHER TAXABLE INTEREST	16,458.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 4A	<14,702.>	

SCHEDULE K-1 SECTION 1231 GAINS(LOSSES)

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
FROM TRADE OR BUSINESS	<30,236.>	SEE FORM 1040 INSTRUCTIONS
TOTAL TO LINE 5	<30,236.>	

SCHEDULE K-1 CHARITABLE CONTRIBUTIONS

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
CHARITABLE CONTRIBUTIONS - 50 % LIMIT	594.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 7	594.	

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<174,033.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 14B	<174,033.>		

BOWE OIL & COAL CO. INC 56-0546791

SCHEDULE K-1 NONDEDUCTIBLE EXPENSES

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	286.	SEE FORM 1040 INSTRUCTIONS
NONDEDUCTIBLE EXPENSES FROM PASS THROUGH ENTITIES	770.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 19	1,056.	

DOJ-018970

SCHEDULE K-1 (Form 1120S)

Shareholder's Share of Income, Credits, Deductions, etc.

▶ See separate instructions.

For calendar year 1999 or tax year beginning ____ and ending ____

1999

Shareholder's identifying number ▶ 56-6188593

Shareholder's name, address, and ZIP code

THE 1999 ROBERT L PIERCE GRANTOR
TRUST B FBO ROBERT C PIERCE
310 BETHEL DRIVE
SALISBURY, NC 28144

Corporation's identifying number ▶ 56-0546791

Corporation's name, address, and ZIP code

HOME OIL & COAL CO INC
P O BOX 139
SALISBURY, NC 28145

A Shareholder's percentage of stock ownership for tax year ▶ 27.197879%

B Internal Revenue Service Center where corporation filed its return ▶ MEMPHIS, TN

C Tax shelter registration number ▶

D Check applicable box: (1) ☐ Final K-1 (2) ☐ Amended K-1

	(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on:
Income (Loss)	1 Ordinary income (loss) from trade or business activities	1	124,297.	See pages 4 and 5 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	2 Net income (loss) from rental real estate activities	2		
	3 Net income (loss) from other rental activities	3		
	4 Portfolio income (loss):			
	a Interest SEE STATEMENT	4a	<14,702.	Sch. B, Part I, line 1
	b Ordinary dividends	4b		Sch. B, Part II, line 5
	c Royalties	4c		Sch. E, Part I, line 4
	d Net short-term capital gain (loss)	4d	30,930.	Sch. D, line 5, col. (f)
	e Net long-term capital gain (loss):			
	(1) 28% rate gain (loss)	e(1)		Sch. D, line 12, col. (g)
	(2) Total for year	e(2)	<44,111.	Sch. D, line 12, col. (f)
	f Other portfolio income (loss) (attach schedule)	4f		Enter on applicable line of your return.
	5 Net section 1231 gain (loss) (other than due to casualty or theft) STMT	5	<30,216.	See Shareholder's Instructions for Schedule K-1 (Form 1120S).
	6 Other income (loss) (attach schedule)	6		Enter on appropriate line of your return.
Deductions	7 Charitable contributions (attach schedule) SEE STATEMENT	7	594.	Sch. A, line 15 or 16
	8 Section 179 expense deduction	8		See page 8 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	9 Deductions related to portfolio income (loss) (attach schedule)	9		
	10 Other deductions (attach schedule)	10		
Investment Interest	11a Interest expense on investment debts	11a		Form 4952, line 1
	b (1) Investment expense included on lines 4a, 4b, 4c, and 4f above	b(1)	<14,702.	See Shareholder's Instructions for Schedule K-1 (Form 1120S).
	(2) Investment expenses included on line 5 above	b(2)		
Credits	12a Credit for alcohol used as fuel	12a		Form 6478, line 10
	b Low-income housing credit:			
	(1) From section 42(j)(5) partnerships for property placed in service before 1990	b(1)		Form 8586, line 5
	(2) Other than on line 12b(1) for property placed in service before 1990	b(2)		
	(3) From section 42(j)(5) partnerships for property placed in service after 1989	b(3)		
	(4) Other than on line 12b(3) for property placed in service after 1989	b(4)		
	c Qualified rehabilitation expenditures related to rental real estate activities	12c		See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	d Credits (other than credits shown on lines 12b and 12c) related to rental real estate activities	12d		
	e Credits related to other rental activities	12e		
	13 Other credits	13		

AWA For Paperwork Reduction Act Notice, see the Instructions for Form 1120S. Schedule K-1 (Form 1120S) 1999

HOSKE OIL & COAL CO INC 56-0546791

	(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on
Adjustments and Tax Preference Items	14 a Depreciation adjustment on property placed in service after 1986	14a	2,057.	See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S) and instructions for Form 6251
	b Adjusted gain or loss SEE STATEMENT	14b	-174,834.	
	c Depletion (other than oil and gas)	14c		
	d (1) Gross income from oil, gas, or geothermal properties	d(1)		
	(2) Deductions allocable to oil, gas, or geothermal properties	d(2)		
	e Other adjustments and tax preference items (attach schedule)	14e		
Foreign Taxes	15 a Type of income ▶			Form 1116, Check boxes
	b Name of foreign country or U.S. possession ▶			
	c Total gross income from sources outside the United States (attach schedule)	15c		Form 1116, Part I
	d Total applicable deductions and losses (attach schedule)	15d		
	e Total foreign taxes (check one): ▶ ☐ Paid ☐ Accrued	15e		Form 1116, Part II
	f Reduction in taxes available for credit (attach schedule)	15f		Form 1116, Part III
	g Other foreign tax information (attach schedule)	15g		See instructions for Form 1116
Other	16 Section 59(e)(2) expenditures: a Type ▶			See Shareholder's Instructions for Schedule K-1 (Form 1120S).
	b Amount	16b		
	17 Tax-exempt interest income	17		Form 1040, line 8b
	18 Other tax-exempt income	18		
	19 Nondeductible expenses SEE STATEMENT	19	1,055.	See pages 7 and 8 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	20 Property distributions (including cash) other than dividend distributions reported to you on Form 1099-DIV	20	3,817,279.	
	21 Amount of loan repayments for "Loans From Shareholders"	21		
	22 Recapture of low-income housing credit:			
	a From section 42(j)(5) partnerships	22a		Form 8611, line 8
	b Other than on line 22a	22b		
Supplemental Information	23 Supplemental information required to be reported separately to each shareholder (attach additional schedules if more space is needed):			

SHAREHOLDER NUMBER 4

15190331 767283 1232 1999.05200 HOSKE OIL & COAL CO INC 1232 1

BOWE OIL & COAL CO INC 56-0546791

SCHEDULE K-1 INTEREST INCOME

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
U.S. GOVERNMENT INTEREST	<31,161.>	SEE FORM 1040 INSTRUCTIONS
OTHER TAXABLE INTEREST	16,459.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 4A	<14,702.>	

SCHEDULE K-1 SECTION 1231 GAINS(LOSSES)

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
FROM TRADE OR BUSINESS	<30,236.>	SEE FORM 1040 INSTRUCTIONS
TOTAL TO LINE 5	<30,236.>	

SCHEDULE K-1 CHARITABLE CONTRIBUTIONS

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
CHARITABLE CONTRIBUTIONS - 50 % LIMIT	594.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 7	594.	

SCHEDULE K-1 ADJUSTED GAIN OR LOSS

ALLOCABLE PORTIONS	TOTAL AMOUNT	25%/28% RATE AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
SECTION 1231 GAIN OR LOSS	<174,034.>		SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 14B	<174,034.>		

DOJ-018973

MORE OIL & COAL CO INC . 56-0546791

SCHEDULE K-1 NONDEDUCTIBLE EXPENSES

DESCRIPTION	AMOUNT	SHAREHOLDER FILING INSTRUCTIONS
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	286.	SEE FORM 1040 INSTRUCTIONS
NONDEDUCTIBLE EXPENSES FROM PASS THROUGH ENTITIES	769.	SEE FORM 1040 INSTRUCTIONS
TOTAL TO SCHEDULE K-1, LINE 18	1,055.	

DOJ-018974

Form 4562 — Depreciation and Amortization (Including Information on Listed Property) OTHER — 1999

▶ See separate instructions. ▶ Attach this form to your return.

Name(s) shown on return: HOWE OIL & COAL CO INC

Business or activity to which this form relates: OTHER DEPRECIATION

Identifying number: 55-0546791

Part I Election To Expense Certain Tangible Property (Section 179) (Note: If you have any "listed property," complete Part V before you complete Part I.)

1 Maximum dollar limitation. If an enterprise zone business, see instructions	1	19,000.
2 Total cost of section 179 property placed in service. See instructions	2	72,106.
3 Threshold cost of section 179 property before reduction in limitation	3	$200,000
4 Reduction in limitation. Subtract line 3 from line 2. If zero or less, enter -0-	4	0.
5 Dollar limitation for tax year. Subtract line 4 from line 1. If zero or less, enter -0-. If married filing separately, see instructions	5	19,000.

6 (a) Description of property	(b) Cost (business use only)	(c) Elected cost

7 Listed property. Enter amount from line 27	7	
8 Total elected cost of section 179 property. Add amounts in column (c), lines 6 and 7	8	
9 Tentative deduction. Enter the smaller of line 5 or line 8	9	
10 Carryover of disallowed deduction from 1998	10	
11 Business income limitation. Enter the smaller of business income (not less than zero) or line 5	11	19,000.
12 Section 179 expense deduction. Add lines 9 and 10, but do not enter more than line 11	12	
13 Carryover of disallowed deduction to 2000. Add lines 9 and 10, less line 12 ▶	13	

Note: Do not use Part II or Part III below for listed property (automobiles, certain other vehicles, certain computers, or property used for entertainment, recreation, or amusement). Instead, use Part V for listed property.

Part II MACRS Depreciation For Assets Placed in Service ONLY During Your 1999 Tax Year (Do Not Include Listed Property.)

Section A - General Asset Account Election

14 If you are making the election under section 168(i)(4) to group any assets placed in service during the tax year into one or more general asset accounts, check this box. See instructions ▶ ☐

Section B - General Depreciation System (GDS) (See instructions.)

(a) Classification of property	(b) Month and year placed in service	(c) Basis for depreciation (Business/investment use only - see instructions)	(d) Recovery period	(e) Convention	(f) Method	(g) Depreciation deduction
15 a 3-year property						
b 5-year property		72,106.	5		HY	200DB 6,004.
c 7-year property						
d 10-year property						
e 15-year property						
f 20-year property						
g 25-year property			25 yrs			S/L
h Residential rental property	/		27.5 yrs		MM	S/L
	/		27.5 yrs		MM	S/L
i Nonresidential real property	/		39 yrs		MM	S/L
	/				MM	S/L

Section C - Alternative Depreciation System (ADS) (See instructions.)

16 a Class life						S/L
b 12-year			12 yrs			S/L
c 40-year	/		40 yrs		MM	S/L

Part III Other Depreciation (Do Not Include Listed Property.) (See instructions.)

17 GDS and ADS deductions for assets placed in service in tax years beginning before 1999	17	111,369.
18 Property subject to section 168(f)(1) election	18	
19 ACRS and other depreciation	19	466.

Part IV Summary (See instructions.)

20 Listed property. Enter amount from line 26	20	759.
21 Total. Add deductions on line 12, lines 15 and 16 in column (g), and lines 17 through 20. Enter here and on the appropriate lines of your return. Partnerships and S corporations - see instructions	21	140,518.
22 For assets shown above and placed in service during the current year, enter the portion of the basis attributable to section 263A costs	22	

LHA For Paperwork Reduction Act Notice, see the separate instructions. Form 4562 (1999)

6

15190331 767285 1232 1999.05200 HOWE OIL & COAL CO INC 1232 1

Form 4562 (1998) CHEROKEE OIL & COAL CO INC 56-0546791 Page 2

Part V Listed Property - Automobiles, Certain Other Vehicles, Cellular Telephones, Certain Computers, and Property Used for Entertainment, Recreation, or Amusement

Note: For any vehicle for which you are using the standard mileage rate or deducting lease expense, complete only 23a, 23b, columns (a) through (c) of Section A, all of Section B, and Section C if applicable.

Section A - Depreciation and Other Information (Caution: See instructions for limits for passenger automobiles.)

24a Do you have evidence to support the business/investment use claimed? [X] Yes [ ] No 24b If "Yes," is the evidence written? [X] Yes [ ] No

(a) Type of property (list vehicles first)	(b) Date placed in service	(c) Business/ investment use percentage	(d) Cost or other basis	(e) Basis for depreciation (business/investment use only)	(f) Recovery period	(g) Method/ Convention	(h) Depreciation deduction	(i) Elected section 179 cost
25 Property used more than 50% in a qualified business use:								
TRUCK 844	022884	10000 %	13,181.	13,181.	5	200DBHY	759.	
		%						
		%						
26 Property used 50% or less in a qualified business use:								
		%				S/L		
		%				S/L		
		%				S/L		
27 Add amounts in column (h). Enter the total here and on line 21, page 1							27 759.	
28 Add amounts in column (i). Enter the total here and on line 7, page 1								28

Section B - Information on Use of Vehicles

Complete this section for vehicles used by a sole proprietor, partner, or other "more than 5% owner," or related person. If you provided vehicles to your employees, first answer the questions in Section C to see if you meet an exception to completing this section for those vehicles.

	(a) Vehicle	(b) Vehicle	(c) Vehicle	(d) Vehicle	(e) Vehicle	(f) Vehicle
29 Total business/investment miles driven during the year (DO NOT include commuting miles)						
30 Total commuting miles driven during the year						
31 Total other personal (noncommuting) miles driven						
32 Total miles driven during the year. Add lines 29 through 31						

	Yes	No	Yes	No	Yes	No	Yes	No	Yes	No	Yes	No
33 Was the vehicle available for personal use during off-duty hours?												
34 Was the vehicle used primarily by a more than 5% owner or related person?												
35 Is another vehicle available for personal use?												

Section C - Questions for Employers Who Provide Vehicles for Use by Their Employees

Answer these questions to determine if you meet an exception to completing Section B for vehicles used by employees who are not more than 5% owners or related persons.

	Yes	No
36 Do you maintain a written policy statement that prohibits all personal use of vehicles, including commuting, by your employees?		X
37 Do you maintain a written policy statement that prohibits personal use of vehicles, except commuting, by your employees? See instructions for vehicles used by corporate officers, directors, or 1% or more owners	X	
38 Do you treat all use of vehicles by employees as personal use?		X
39 Do you provide more than five vehicles to your employees, obtain information from your employees about the use of the vehicles, and retain the information received?		X
40 Do you meet the requirements concerning qualified automobile demonstration use?		X

Note: If your answer to 36, 37, 38, 39, or 40 is "Yes," you need not complete Section B for the covered vehicles.

Part VI Amortization

(a) Description of costs	(b) Date amortization begins	(c) Amortizable amount	(d) Code section	(e) Amortization period or percentage	(f) Amortization for this year
42 Amortization of costs that begins during your 1998 tax year:					
43 Amortization of costs that began before 1998				43	
44 Total. Enter here and on "Other Deductions" or "Other Expenses" line of your return				44	

Form 4562 (1998)

15190331 767281 1232 1998.05200 CHEROKEE OIL & COAL CO INC 1233 1
Case 7:06-cv-00181-FL Document 27-9 Filed 04/19/07 Page 24 of 32
DOJ-018976

Form **4797**

Department of the Treasury
Internal Revenue Service (99)

Sales of Business Property

(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))

▶ Attach to your tax return.

1999

Attachment Sequence No. **27**

Name(s) shown on return

MINER OIL & COAL CO INC

Identifying number

56-0546791

1 Enter the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or substitute statement) that you will be reporting on line 2, 10, or 20 1

Part I **Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft - Property Held More Than 1 Year**

(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) Gain or (loss) Subtract (f) from the sum of (d) and (e)
1 PASSTHROUGH FROM MINER CONCRETE & SUPPLY LLC						<110,362.>

3	Gain, if any, from Form 4684, line 39	3
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5
6	Gain, if any, from line 32, from other than casualty or theft	6
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows:	7 <110,362.>
	Partnerships (except electing large partnerships). Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 9. Skip lines 8, 9, 11, and 12 below.	
	S corporations. Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax.	
	All others. If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	
8	Nonrecaptured net section 1231 losses from prior years (see instructions)	8
9	Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line as follows (see instructions):	9
	S corporations. Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below.	
	All others. If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D.	

Part II **Ordinary Gains and Losses**

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):						

11	Loss, if any, from line 7	11
12	Gain, if any, from line 7 or amount from line 8, if applicable	12
13	Gain, if any, from line 31	13 89,065.
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations (see instructions)	17
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18 89,065.
	a For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.	
	b For individual returns:	
	(1) If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)." See instructions	18b(1)
	(2) Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)

JSA For Paperwork Reduction Act Notice, see separate instructions. Form **4797** (1999)

DOJ-018977

ROWE OIL & COAL CO INC 55-0546791

Form 4562 (1996) Page 2

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:					(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A SALE OF PICKUP TRUCK #18					100185	040199
B SALE OF #18 OIL TRUCK					050173	050699
C SALE OF ROLLER & CRIMPER					050166	052199
D SALE OF TRUCK # 27					VARIES	020299
These columns relate to the properties on lines 19A through 19D.		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20	560.	1,500.	10.	22,925.
21 Cost or other basis plus expense of sale	21	11,341.	12,767.	90.	80,058.
22 Depreciation (or depletion) allowed or allowable	22	11,341.	12,767.	90.	79,228.
23 Adjusted basis. Subtract line 22 from line 21	23	0.	0.	0.	830.
24 Total gain. Subtract line 23 from line 20	24	560.	1,500.	10.	22,095.
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	11,341.	12,767.	90.	79,228.
b Enter the smaller of line 24 or 25a	25b	560.	1,500.	10.	22,095.
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26b from line 24. If residential rental property or line 24 is not more than line 26b, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	89,065.
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	89,065.
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 6781, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

See instructions.

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See instructions for where to report	35		

BOWIE OIL & COAL CO INC

56-0546791

Part III

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:					
A SALE OF OIL EQUIPMENT TO KNIGHT OIL					VARIES 041299
B					
C					
D					

		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20	65,000.			
21 Cost or other basis plus expense of sale	21	206,834.			
22 Depreciation (or depletion) allowed or allowable	22	206,734.			
23 Adjusted basis. Subtract line 22 from line 21	23	100.			
24 Total gain. Subtract line 23 from line 20	24	64,900.			
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a	206,734.			
b Enter the smaller of line 24 or 25a	25b	64,900.			
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less (see instructions)

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation. See instructions	34		
35 Recapture amount. Subtract line 34 from line 33. See instructions for where to report	35		

Case 7:06-cv-00181-AC Document 27-4 Filed 04/19/07 Page 27 of 32

1999 Income from Passthroughs

[redacted] CONCRETE & SUPPLY LLC
I.D. [redacted]: 56-2136387
TYPE: PARTNERSHIP

ORDINARY INCOME (LOSS)	-785,062	
TAX PREFERENCE ITEMS:		
DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY		202,995
ADJUSTED GAIN OR LOSS		-635,227
OTHER K-1 INFORMATION:		
INTEREST		16,750
SHORT-TERM CAPITAL GAIN (LOSS) - PORTFOLIO		112,896
LONG-TERM CAPITAL GAIN (LOSS) - PORTFOLIO		-161,537
SECTION 1231 GAIN (LOSS)		-110,362
NONDEDUCTIBLE EXPENSES		2,808
U.S. BOND INTEREST		-113,737

HOME OIL & COAL CO INC 56-0546791

FORM 1120S	OTHER INCOME	STATEMENT 1
DESCRIPTION		AMOUNT
HOME CONCRETE & SUPPLY LLC		<785,842.>
PAYMENT FROM LLC FOR COMMON PAYMASTER SERVICE		333,953.
SERVICE CHARGES		3,282.
MISCELLANEOUS		50,601.
481 (A) ADJUSTMENT FOR 263A INVENTORY CHARGE		13,307.
TOTAL TO FORM 1120S, PAGE 1, LINE 5		<383,899.>

FORM 1120S	TAXES AND LICENSES	STATEMENT 2
DESCRIPTION		AMOUNT
FICA		87,743.
FUTA		3,179.
SUTA		1,366.
FRANCHISE TAX		7,395.
SALES TAX		<9,533.>
TOTAL TO FORM 1120S, PAGE 1, LINE 12		90,150.

FORM 1120S	OTHER DEDUCTIONS	STATEMENT 3
DESCRIPTION		AMOUNT
UTILITIES		13,366.
TELEPHONE		6,523.
INSURANCE		45,356.
OFFICE EXPENSE		26,729.
TRAVEL		2,095.
TRUCK EXPENSE		85,122.
LEGAL & PROFESSIONAL		119,711.
CONTRACT LABOR		7,663.
PENSION PLAN ADMINISTRATION		800.
SUPPLIES		3,038.
CASH OVER AND SHORT		15,325.
DUES & SUBSCRIPTIONS		4,033.
REFUNDS		10,662.
DISCOUNTS		15,591.
RETURNED CHECKS		13,166.
CONCRETE WARRANTY EXPENSE		5,100.
MISCELLANEOUS		118.
UNIFORMS		5,300.

BOMB OIL & COAL CO INC	56-0546791
DIRECTOR FEES	20,250.
ENVIRONMENTAL EXPENSE	6,671.
MEALS AND ENTERTAINMENT	1,043.
TOTAL TO FORM 1120S, PAGE 1, LINE 19	607,642.

FORM 1120S — CHANGES IN SHAREHOLDER INTERESTS — STATEMENT 4

TOTAL NUMBER OF DAYS IN THE TAX YEAR: 365
TOTAL NUMBER OF SHARES OUTSTANDING AT THE END OF THE YEAR: 5,300.00

SHAREHOLDER NAME AND ID NUMBER	PERIOD HELD FROM - TO	DAYS	NUMBER OF SHRS HELD	PCT. OF STOCK OWNED	ALLOC. PERCENT	SHARE-HOLDER TOTAL
ROBERT L PIERCE 248-60-2595						
	01/01/99 - 04/26/99	116	4,300.00	81.132	25.784	
	04/27/99 - 12/31/99	249	43.00	0.811	0.553	26.34
STEPHEN R CHANDLER 246-72-2482						
	01/01/99 - 04/26/99	116	1,000.00	18.868	5.996	
	04/27/99 - 12/31/99	249	1,000.00	18.868	12.872	18.87
THE 1999 ROBERT L PIERCE GRANTOR TRU 58-6388593						
	01/01/99 - 04/26/99	116	0.00	0.000	0.000	
	04/27/99 - 12/31/99	249	2,128.50	40.160	27.397	27.40
THE 1999 ROBERT L PIERCE GRANTOR TRUS 58-6388593						
	01/01/99 - 04/26/99	116	0.00	0.000	0.000	
	04/27/99 - 12/31/99	249	2,128.50	40.160	27.397	27.40

Case 7:06-cv-00181-FL Document 27-4 Filed 04/19/07 Page 30 of 32
DOJ-018982

HOME OIL & COAL CO INC 56-0546791

SCHEDULE K INTEREST INCOME STATEMENT 5

DESCRIPTION	US	OTHER
VARIOUS BANKS	0.	43,326.
INTEREST FROM HOME CONCRETE & SUPPLY LL	0.	16,750.
HOME CONCRETE & SUPPLY LLC	<113,737.>	0.
TOTAL TO SCHEDULE K, LINE 4A	<113,737.>	60,076.

SCHEDULE K NET GAIN (LOSS) UNDER SECTION 1231 STATEMENT 6

DESCRIPTION	AMOUNT
SECTION 1231 GAIN (LOSS) FROM TRADE/BUSINESS	<110,362.>
TOTAL TO SCHEDULE K, LINE 5	<110,362.>

SCHEDULE K CHARITABLE CONTRIBUTIONS STATEMENT 7

DESCRIPTION	50% LIMIT	30% LIMIT	20% LIMIT
FRANKLIN PRESBYTERIAN CHURCH	25.		
CLOSE UP	55.		
MILFORD HILLS UNITED METHODIST CHURCH	324.		
MARCH OF DIMES	50.		
ST MARKS LUTHERAN CHURCH	25.		
SALISBURY KIWANIS	100.		
CENTRAL NC COUNCIL BOY SCOUTS	100.		
ROMAN BUSINESS FORMS	75.		
ROTARY EDUCATION FOUNDATION	100.		
CAMP MANA	50.		
HABITAT FOR HUMANITY	312.		
MISC	138.		
UNITED ARTS COUNCIL	50.		
WITTENBERG LUTHERAN CHURCH	306.		
CHRIST ASSIST NETWORK	223.		
SALVATION ARMY	11.		
ROWAN COUNTY SHERIFFS DEPT	50.		
ROWAN ROSE SOCIETY	25.		
SALISBURY CIVITAN CHARITES	150.		
TOTALS TO SCHEDULE K, LINE 7	2,169.		

SOME OIL & COAL CO INC 56-0546791

SCHEDULE K	ADJUSTED GAIN OR LOSS	STATEMENT 8
DESCRIPTION	TOTAL AMOUNT	25%/28% RATE AMOUNT
FROM PASSTHROUGH - SECTION 1231	<635,227.>	0.
TOTAL TO SCHEDULE K, LINE 14B	<635,227.>	0.

ADJUSTED GAIN OR LOSS ALLOCABLE TO:

ORDINARY GAIN OR LOSS	
SECTION 1231 GAIN OR LOSS	<635,227.>
SHORT-TERM CAPITAL GAIN OR LOSS	
LONG-TERM CAPITAL GAIN OR LOSS	
UNRECAPTURED SECTION 1250 GAIN - 25% RATE AMOUNT	

SCHEDULE K	NONDEDUCTIBLE EXPENSES	STATEMENT 9
DESCRIPTION		AMOUNT
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES		1,043.
NONDEDUCTIBLE EXPENSES FROM PASSTHROUGH ENTITIES		2,808.
TOTAL TO SCHEDULE K, LINE 19		3,851.

SCHEDULE K	OTHER ITEMS, LINE 21	STATEMENT 10
DESCRIPTION		AMOUNT
MEDICAL INSURANCE PREMIUMS		1,462.
MEDICAL INSURANCE PREMIUMS		1,462.

SCHEDULE M-2 ACCUMULATED ADJUSTMENTS ACCOUNT - OTHER ADDITIONS	STATEMENT 11
DESCRIPTION	AMOUNT
ADDITIONAL INVESTMENT IN SOME CONCRETE & SUPPLY BY STOCKHOLDERS	5,925,453.
SHORT-TERM CAPITAL GAIN - SCHEDULE D	112,896.
BAD DEBT DIFFERENCE	
263A PRIOR YEAR INVENTORY ADJUSTMENT	63,320.
INTEREST INCOME	<53,663.>
TOTAL TO SCHEDULE M-2, LINE 3 - COLUMN (A)	6,048,006.

DOJ-018984

HOME OIL & COAL CO INC 56-0546791

SCHEDULE M-2 ACCUMULATED ADJUSTMENTS ACCOUNT- OTHER REDUCTIONS STATEMENT 12

DESCRIPTION	AMOUNT
CHARITABLE CONTRIBUTIONS	2,169.
SECTION 1231 LOSSES	110,362.
263A CURRENT YEAR INVENTORY ADJUSTMENT	13,307.
OFFICERS LIFE INSURANCE	7,307.
DIFFERENCE IN BAD DEBT ALLOWANCE & ACTUAL	5,000.
NONDEDUCTIBLE EXPENSES FROM PASSTHROUGH ENTITIES	2,808.
EXCLUDED MEALS AND ENTERTAINMENT EXPENSES	1,043.
LONG-TERM CAPITAL LOSS - SCHEDULE D	161,079.
TOTAL TO SCHEDULE M-2, LINE 5 - COLUMN (A)	303,075.

SCHEDULE L OTHER CURRENT ASSETS STATEMENT 13

DESCRIPTION	BEGINNING OF TAX YEAR	END OF TAX YEAR
PREPAID INSURANCE	53,060.	
CASH VALUE OF LIFE INSURANCE	95,337.	
IRSA STOCK	8,215.	
INTERCOMPANY RECEIVABLE		258,138.
TOTAL TO SCHEDULE L, LINE 6	156,612.	258,138.

SCHEDULE L OTHER INVESTMENTS STATEMENT 14

DESCRIPTION	BEGINNING OF TAX YEAR	END OF TAX YEAR
INVESTMENT IN HOME CONCRETE & SUPPLY LLC		696,289.
TOTAL TO SCHEDULE L, LINE 9		696,289.

Case 7:06-cv-00181-FL Document 27-5 Filed 04/19/07 Page 1 of 33

DOJ-018985

HOKE OIL & COAL CO INC 56-0546791

SCHEDULE L OTHER CURRENT LIABILITIES STATEMENT 15

DESCRIPTION	BEGINNING OF TAX YEAR	END OF TAX YEAR
FUTA PAYABLE	112.	
SUTA PAYABLE	50.	
ACCRUED OTHER TAXES	32,646.	
ACCRUED SALARIES	261,719.	
401 K WITHHOLDING PAYABLE	21,322.	
FED W/H & FICA PAYABLE	65,305.	
STATE W/H PAYABLE	8,990.	
TOTAL TO SCHEDULE L, LINE 18	370,144.	

SCHEDULE M-1 TAXABLE INCOME NOT RECORDED ON BOOKS STATEMENT 16

DESCRIPTION	AMOUNT
263A CURRENT YEAR INVENTORY ADJUSTMENT	13,307.
TOTAL TO SCHEDULE M-1, LINE 2	13,307.

SCHEDULE M-1 EXPENSES RECORDED ON BOOKS BUT NOT DEDUCTED ON RETURN STATEMENT 17

DESCRIPTION	AMOUNT
NON-DEDUCTIBLE EXPENSES FROM PASSTHROUGH ENTITIES	2,808.
OFFICERS LIFE INSURANCE	7,307.
DIFFERENCE IN BAD DEBT ALLOWANCE & ACTUAL	5,000.
TOTAL TO SCHEDULE M-1, LINE 3	15,115.

HOME OIL & COAL CO.INC 56-0546791

SCHEDULE M-1 DEDUCTIONS ON RETURN NOT CHARGED AGAINST BOOK INCOME STATEMENT 18

DESCRIPTION	AMOUNT
BAD DEBT DIFFERENCE 263A PRIOR YEAR INVENTORY ADJUSTMENT	63,320.
TOTAL TO SCHEDULE M-1, LINE 6	63,320.

SCHEDULE L ANALYSIS OF TOTAL RETAINED EARNINGS PER BOOKS STATEMENT 19

DESCRIPTION	AMOUNT
BALANCE AT BEGINNING OF YEAR - SCHEDULE L, LINE 24, COLUMN (B)	4,879,189.
NET INCOME PER BOOKS - SCHEDULE M-1, LINE 1	273,165.
DISTRIBUTIONS	<9,760,145.>
OTHER INCREASES (DECREASES)	
ADDITIONAL INVESTMENT IN HOME CONCRETE & SUPPLY BY STOCKHOLDERS	5,925,453.
BALANCE AT END OF YEAR - SCHEDULE L, LINE 24, COLUMN (D)	1,317,662.

DOJ-016987

Transferor's Statement under
Reg 1.351-3(a)
Home Oil & Coal Company
SSN 66-0646791
From 11306, Tax Year Ending 12/31/1999

1. Description of property transferred.

a. Property transferred by Robert L. Pierce June 14, 1999

Property
.0158% Interest in Home Concrete Supply LLC EIN 86-0126307

b. Property transferred by Stephen B. Chandler June 14, 1999

Property
.3067% Interest in Home Concrete Supply LLC EIN 86-0126307

c. Property transferred by The 1999 Robert L Pierce Grantor Trust
UIA dtd. 4/21/99 Trust A FBO Julie Margaret Pierce on June 14, 1999

Property
.6031% Interest in Home Concrete Supply LLC EIN 86-0126307

d. Property transferred by The 1999 Robert L Pierce Grantor Trust
UIA dtd. 4/21/99 Trust B FBO Robert Cade Pierce on June 14, 1999

Property
.6031% Interest in Home Concrete Supply LLC EIN 86-0126307

2. Cost or basis in hands of transferor as of date of transfer

a. Robert L. Pierce	$ 98,891.14
b. Stephen B. Chandler	$ 1,138,398.13
c. The 1999 Robert L Pierce Grantor Trust UIA dtd 4/21/99 Trust A FBO Julie Margaret Pierce on June 14, 1999	$ 2,363,331.83
d. The 1999 Robert L Pierce Grantor Trust UIA dtd 4/21/99 Trust A FBO Robert Cade Pierce on June 14, 1999	$ 2,363,331.83

3. a. Total issued and outstanding capital stock immediately prior to the exchange 5,300

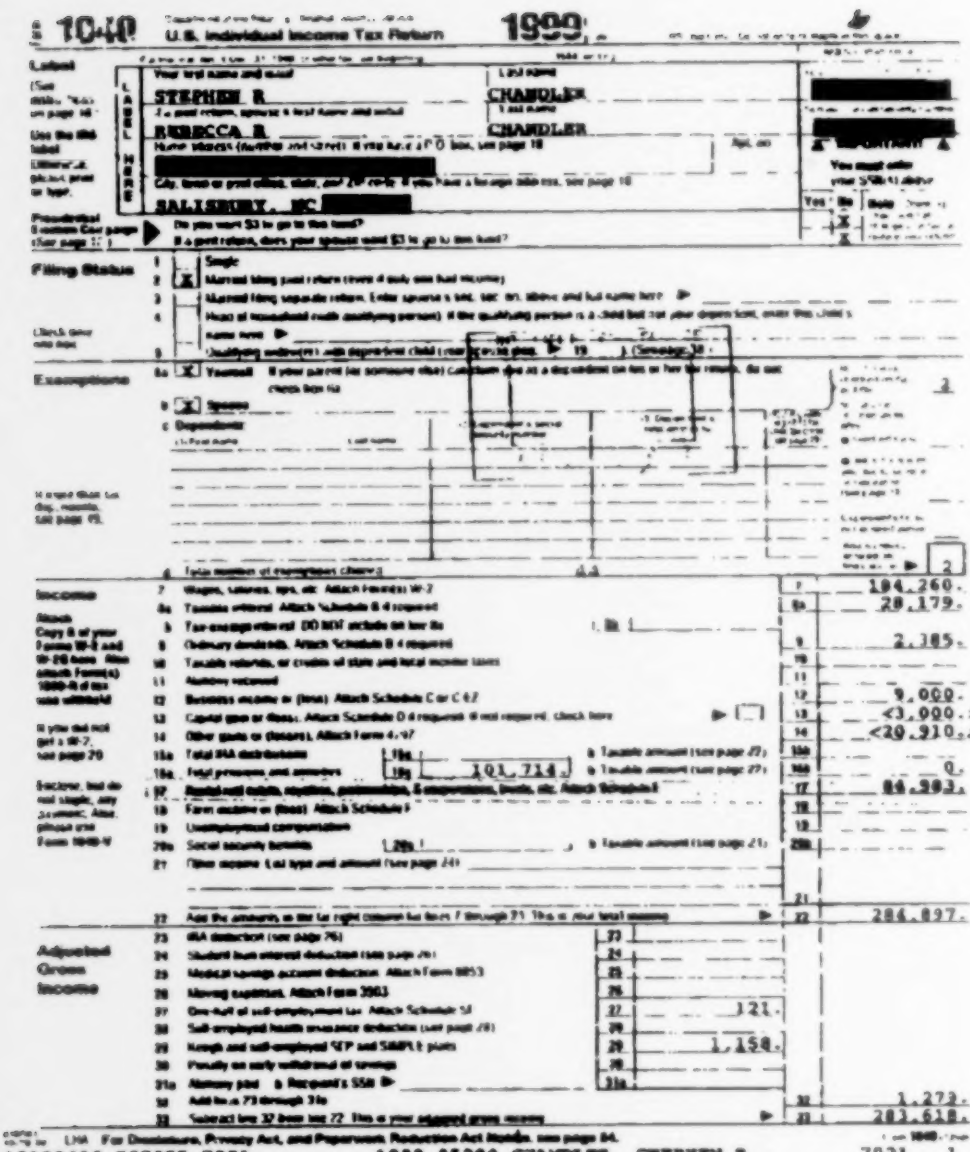
b. Total issued and outstanding capital stock immediately after the exchange 5,300

c. Stock issued in the exchange None

Shares owned by transferor immediately prior to and after the exchange

Transferee's Statement under
Reg 1.351-3(b)
Name Oil & Coal Company
EIN 00-0000701
From 11/30/, Tax Year Ending 12/31/1999

	a. Robert L. Pierce	43
	b. Stephen S. Chandler	1,000
	c. The 1999 Robert L Pierce Grantor Trust UA dtd 4/21/99 Trust A FBO Julie Sherwood Pierce on June 14, 1999	2,139.5
	d. The 1999 Robert L Pierce Grantor Trust UA dtd 4/21/99 Trust A FBO Robert Craig Pierce on June 14, 1999	2,139.5
	iii. Fair market value of stock issued to transferors	Not applicable
4.	i. Principal amount and terms of all securities assumed immediately prior to and immediately after the exchange	Not applicable
	ii. Principal amount and terms of all securities issued to transferors in the exchange and the transferor's holdings of securities immediately prior to and immediately after the exchange	Not applicable
	iii. Fair market value of securities issued to transferors	Not applicable
5.	Amount of money assumed by transferors	None
6.	Other property which was assumed by transferors	None
7.	Liabilities assumed by the controlled corporation in the exchange	None



Form 1040 U.S. Individual Income Tax Return 1999

Label
Your first name and initial: STEPHEN R
Last name: CHANDLER
If a joint return, spouse's first name and initial: REBECCA B
Last name: CHANDLER
Home address (number and street): [redacted]
City, town or post office, state, and ZIP code: SALISBURY, NC [redacted]
Use the IRS label. Otherwise, please print or type.
Presidential Election Campaign (See page 17)
Do you want $3 to go to this fund? Yes X
If a joint return, does your spouse want $3 to go to this fund? No X
You must enter your SSN(s) above

Filing Status
1 Single
2 X Married filing joint return (even if only one had income)
3 Married filing separate return. Enter spouse's SSN above and full name here.
4 Head of household (with qualifying person). (See page 17.) If the qualifying person is a child but not your dependent, enter this child's name here.
5 Qualifying widow(er) with dependent child (year spouse died ▶ 19). (See page 17.)

Exemptions
6a X Yourself. If your parent (or someone else) can claim you as a dependent on his or her tax return, do not check box 6a. 1
b X Spouse 1
c Dependents: (1) First name / Last name; (2) If child under age 1 born in 1999, enter date of birth; (3) Dependent's relationship to you; (4) Number of months lived in your home in 1999; (5) Did dependent have income of $2,750 or more? (See page 18.)
If more than six dependents, see page 19.
d Total number of exemptions claimed 2

Income
Attach Copy B of your Forms W-2 and W-2G here. Also attach Form(s) 1099-R if tax was withheld.
If you did not get a W-2, see page 20.
Enclose, but do not staple, any payment. Also, please use Form 1040-V.

7	Wages, salaries, tips, etc. Attach Form(s) W-2	7	194,260.
8a	Taxable interest. Attach Schedule B if required	8a	28,179.
b	Tax-exempt interest. DO NOT include on line 8a	8b	
9	Ordinary dividends. Attach Schedule B if required	9	2,385.
10	Taxable refunds, or credits of state and local income taxes	10	
11	Alimony received	11	
12	Business income or (loss). Attach Schedule C or C-EZ	12	9,000.
13	Capital gain or (loss). Attach Schedule D if required. If not required, check here ▶ ☐	13	<3,000.>
14	Other gains or (losses). Attach Form 4797	14	<20,910.>
15a	Total IRA distributions 15a	b Taxable amount (see page 27)	15b	0.
16a	Total pensions and annuities 16a 101,714.	b Taxable amount (see page 27)	16b	84,393.
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E	17	
18	Farm income or (loss). Attach Schedule F	18	
19	Unemployment compensation	19	
20a	Social security benefits 20a	b Taxable amount (see page 31)	20b	
21	Other income. List type and amount (see page 31)	21	
22	Add the amounts in the far right column for lines 7 through 21. This is your total income ▶	22	284,897.

Adjusted Gross Income

23	IRA deduction (see page 29)	23	
24	Student loan interest deduction (see page 29)	24	
25	Medical savings account deduction. Attach Form 8853	25	
26	Moving expenses. Attach Form 3903	26	
27	One-half of self-employment tax. Attach Schedule SE	27	121.
28	Self-employed health insurance deduction (see page 29)	28	
29	Keogh and self-employed SEP and SIMPLE plans	29	1,152.
30	Penalty on early withdrawal of savings	30	
31a	Alimony paid b Recipient's SSN ▶	31a	
32	Add lines 23 through 31a	32	1,273.
33	Subtract line 32 from line 22. This is your adjusted gross income ▶	33	283,618.

For Disclosure, Privacy Act, and Paperwork Reduction Act Notice, see page 84. Form 1040 (1999)

15190406 767285 7021 1999.0520^ CHANDLER, STEPHEN R 7021 1

STEPHEN R & [redacted] A R CHANDLER

Tax and Credits	34	Amount from line 33 (adjusted gross income)		293,618.
	35a	Check if: You were 65 or older, Blind; Spouse was 65 or older, Blind. Add the number of boxes checked and enter the total here ▶ 35a		
Standard Deduction for Most People	b	If you are married filing separately and your spouse itemizes deductions, or you were a dual-status alien, see page 32 and check here ▶ 35b		
	36	Itemized deductions (from Schedule A) or your standard deduction (see left margin)	36	43,814.
	37	Subtract line 36 from line 34	37	249,804.
	38	If line 34 is $94,975 or less, multiply $3,200 by the total number of exemptions claimed on line 6d. If line 34 is over $94,975, see the worksheet on page 33 for the amount to enter	38	1,320.
	39	Taxable income. Subtract line 38 from line 37. If line 38 is more than line 37, enter -0-	39	248,484.
Married Filing Jointly or Qualifying Widow(er) $7,850 Married Filing Separately $3,925	40	Tax (see page 33). Check if any tax is from: a [ ] Form(s) 8814 b [ ] Form 4972	40	69,209.
	41	Credit for child and dependent care expenses. Attach Form 2441	41	
	42	Credit for the elderly or the disabled. Attach Schedule R	42	
	43	Child tax credit (see page 33)	43	
	44	Education credits. Attach Form 8863	44	
	45	Adoption credit. Attach Form 8839	45	
	46	Foreign tax credit. Attach Form 1116 if required	46	
	47	Other credits. Check if from: a [ ] Form 3800 b [ ] Form 8396 c [ ] Form 8801 d [ ] Form (specify)	47	
	48	Add lines 41 through 47. These are your total credits	48	
	49	Subtract line 48 from line 40. If line 48 is more than line 40, enter -0-	49	69,209.
Other Taxes	50	Self-employment tax. Attach Schedule SE	50	24.
	51	Alternative minimum tax. Attach Form 6251	51	0.
	52	Social security and Medicare tax on tip income not reported to employer. Attach Form 4137	52	
	53	Tax on IRAs, other retirement plans, and MSAs. Attach Form 5329 if required	53	
	54	Advance earned income credit payments from Form(s) W-2	54	
	55	Household employment taxes. Attach Schedule H	55	
	56	Add lines 49 through 55. This is your total tax	56	69,450.
Payments	57	Federal income tax withheld from Forms W-2 and 1099	57 59,180.	
	58	1998 estimated tax payments and amount applied from 1997 return	58 100,160.	
	59a	Earned income credit. Attach Sch. EIC if you have a qualifying child		
	b	Nontaxable earned income: amount ▶ and type ▶	59a	
	60	Additional child tax credit. Attach Form 8812	60	
	61	Amount paid with request for extension to file (see page 62)	61	
	62	Excess social security and RRTA tax withheld (see page 48) STMT 6	62 2,016.	
	63	Other payments. Check if from: a [ ] Form 2439 b [ ] Form 4136	63	
	64	Add lines 57, 58, 59a, and 60 through 63. These are your total payments ▶	64	152,356.
Refund	65	If line 64 is more than line 56, subtract line 56 from line 64. This is the amount you OVERPAID	65	82,906.
	66a	Amount of line 65 you want REFUNDED TO YOU ▶	66a	
	b	Routing number ▶ c Type: [ ] Checking [ ] Savings		
	d	Account number		
	67	Amount of line 65 you want APPLIED TO YOUR 1999 ESTIMATED TAX ▶ 67	82,906.	
Amount You Owe	68	If line 56 is more than line 64, subtract line 64 from line 56. This is the AMOUNT YOU OWE. For details on how to pay, see page 63 ▶	68	
	69	Estimated tax penalty. Also include on line 68 ▶ 69		

Sign Here — Joint return? See page 17. Keep a copy for your records.

[redacted] 4/15/00 EXECUTIVE 204-636-4211

[redacted] 4/15/00 NURSE

Paid Preparer's Use Only — Preparer's signature ▶ [redacted] Date 04/06/00 Check if self-employed [ ] Preparer's SSN or PTIN P00066226

Firm's name (or yours if self-employed) ▶ SHERRILL & SMITH, CPAS, PA EIN 56-2156279

Address ▶ 524 WEST INNES STREET ZIP code 28144

SALISBURY, NC

5

15190406 767285 7021 1999.05200 CHANDLER, STEPHEN R 7021 1

Case 7:06-cv-00181-FL Document 26-6 Filed 04/19/07 Page 2 of 28

SCHEDULES A&B (Form 1040)

Schedule A - Itemized Deductions

(Schedule B is on page 2)

▶ Attach to Form 1040. ▶ See instructions for Schedules A and B (Form 1040).

1999

STEPHEN R & REBECCA R CHANDLER

[redacted]

Medical and Dental Expenses		Caution: Do not include expenses reimbursed or paid by others.			
	1	Medical and dental expenses (see page A-1) SEE STATEMENT 5	1	7,051.	
	2	Enter amount from Form 1040, line 34 | 2 | 283,618.			
	3	Multiply line 2 above by 7.5% (.075)	3	21,271.	
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter 0		4	0.
Taxes You Paid (See page A-2)	5	State and local income taxes SEE STATEMENT 7	5	36,377.	
	6	Real estate taxes (see page A-2)	6	1,484.	
	7	Personal property taxes	7	155.	
	8	Other taxes. List type and amount ▶	8		
	9	Add lines 5 through 8		9	38,016.
Interest You Paid (See page A-3)	10	Home mortgage interest and points reported to you on Form 1098	10	5,187.	
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see page A-3 and show that person's name, identifying no., and address ▶	11		
Note: Personal interest is not deductible	12	Points not reported to you on Form 1098. (See page A-3.)	12		
	13	Investment interest. Attach Form 4952 if required. (See page A-3.)	13		
	14	Add lines 10 through 13		14	5,187.
Gifts to Charity If you made a gift and got a benefit for it, see page A-4.	15	Gifts by cash or check. If you made any gift of $250 or more, see page A-4 SEE STATEMENT 8	15	1,197.	
	16	Other than by cash or check. If any gift of $250 or more, see page A-4. You MUST attach Form 8283 if over $500	16	4,125.	
	17	Carryover from prior year	17		
	18	Add lines 15 through 17		18	5,322.
Casualty and Theft Losses	19	Casualty or theft loss(es). Attach Form 4684. (See page A-5.)		19	
Job Expenses and Most Other Miscellaneous Deductions	20	Unreimbursed employee expenses - job travel, union dues, job education, etc. You MUST attach Form 2106 or 2106-EZ if required. (See page A-5.) ▶UNION AND PROFESSIONAL DUES 50.	20	50.	
	21	Tax preparation fees	21		
	22	Other expenses - investment, safe deposit box, etc. List type and amount ▶			
(See page A-5 for expenses to deduct here.)			22		
	23	Add lines 20 through 22	23	50.	
	24	Enter amount from Form 1040, line 34 | 24 | 283,618.			
	25	Multiply line 24 above by 2% (.02)	25	5,672.	
	26	Subtract line 25 from line 23. If line 25 is more than line 23, enter 0		26	0.
Other Miscellaneous Deductions	27	Other - from list on page A-6. List type and amount ▶		27	
Total Itemized Deductions	28	Is Form 1040, line 34, over $126,600 (over $63,300 if married filing separately)? ☐ NO. Your deduction is not limited. Add the amounts in the far right column for lines 4 through 27. Also, enter on Form 1040, line 36. ☒ YES. Your deduction may be limited. See page A-6 for the amount to enter.	STMT 10	▶ 28	43,816.

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule A (Form 1040) 1999

6

15190406 767285 7021 1999.05200 CHANDLER, STEPHEN R 7021 1

STEPHEN R & REBECCA B CHANDLER

Schedule B - Interest and Ordinary Dividends

Part I Interest

1 List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see page B-1 and list this interest first. Also, show that buyer's social security number and address ▶

		Amount
CENTRAL CAROLINA BANK		31.
FARMERS & MERCHANTS BANK		13,919.
FARMERS & MERCHANTS BANK		2,579.
FT ALEX BROWN (GOODNIGHT INVESTMENTS)		21,852.
FROM K-1 - HOME OIL & COAL CO		11,315.
FROM K-1 - HOME CONCRETE & SUPPLY LLC	1	13.
FROM K-1 - HOME OIL & COAL CO		<21,460.>
FROM K-1 - HOME CONCRETE & SUPPLY LLC		<90.>

Note. If you received a Form 1099-INT, Form 1099-OID, or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.

2 Add the amounts on line 1 — 2 — 28,179.

3 Excludable interest on series EE and I U.S. savings bonds issued after 1989 from Form 8815, line 14. You MUST attach Form 8815 — 3

4 Subtract line 3 from line 2. Enter the result here and on Form 1040, line 8a ▶ — 4 — 28,179.

Part II Ordinary Dividends

5 List name of payer. Include only ordinary dividends. If you received any capital gain distributions, see the instructions for Form 1040, line 13 ▶

		Amount
CCB FINANCIAL CORP		
F&M FINANCIAL CORP		260.
FOOD LION A		13.
FOOD LION A		26.
FOOD LION A		44.
FOOD LION B		14.
INNES STREET FINANCIAL CORP		150.
DELHAIZE AMERICA INC CLASS A		2.
DELHAIZE AMERICA INC CLASS A	5	4.
DELHAIZE AMERICA INC CLASS B		5.
CHARLES SCHWAB		1,867.

Note. If you received a Form 1099-DIV or substitute statement from a brokerage firm, list the firm's name as the payer and enter the ordinary dividends shown on that form.

6 Add the amounts on line 5. Enter the total here and on Form 1040, line 9 — 6 — 2,185.

Part III Foreign Accounts and Trusts

You must complete this part if you (a) had over $400 of interest or ordinary dividends; (b) had a foreign account; or (c) received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

	Yes	No
7a At any time during 1999, did you have an interest in or a signature or other authority over a financial account in a foreign country, such as a bank account, securities account, or other financial account?		X
b If "Yes," enter the name of the foreign country ▶		
8 During 1999, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust? If "Yes," you may have to file Form 3520. See page B-2		X

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule B (Form 1040) 1999

15190406 767285 7021 1999.05200 CHANDLER, STEPHEN R 7021 1

SCHEDULE C-EZ (Form 1040)

Net Profit From Business

(Sole Proprietorship)

▶ Partnerships, joint ventures, etc., must file Form 1065 or 1065-B
▶ Attach to Form 1040 or Form 1041 ▶ See instructions

OMB No. 1545-0074

1999

Attachment Sequence No. 09A

Name of proprietor

STEPHEN R CHANDLER

Social security number (SSN)

[redacted]

Part I General Information

You May Use Schedule C-EZ Instead of Schedule C Only If You:

- Had business expenses of $2,400 or less
- Use the cash method of accounting
- Did not have an inventory at any time during the year
- Did not have a net loss from your business
- Had only one business as a sole proprietor

And You:

- Had no employees during the year
- Are not required to file Form 4562, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-3 to find out if you must file
- Do not deduct expenses for business use of your home
- Do not have prior year unallowed passive activity losses from this business

A Principal business or profession, including product or service

SERVICE

B Enter code from pages C-6 & 7

▶ 999999

C Business name. If no separate business name, leave blank.

STEPHEN R CHANDLER, DIRECTOR

D Employer ID number (EIN), if any

E Business address (including suite or room no.). Address not required if same as on Form 1040, page 1

City, town or post office, state, and ZIP code

Part II Figure Your Net Profit

1	Gross receipts. Caution: If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see Statutory Employees in the instructions for Schedule C, line 1, on page C-3 and check here ▶ ☐ SEE STATEMENT 11 ▶	1	9,000.
2	Total expenses. If more than $2,500, you must use Schedule C. See instructions	2	0.
3	Net profit. Subtract line 2 from line 1. If less than zero, you must use Schedule C. Enter on Form 1040, line 12, and also on Schedule SE, line 2. (Statutory employees do not report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)	3	9,000.

Part III Information on Your Vehicle. Complete this part ONLY if you are claiming car or truck expenses on line 2.

4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ / /

5 Of the total number of miles you drove your vehicle during 1999, enter the number of miles you used your vehicle for:

a Business _____ b Commuting _____ c Other _____

6 Do you (or your spouse) have another vehicle available for personal use? ☐ Yes ☐ No

7 Was your vehicle available for use during off-duty hours? ☐ Yes ☐ No

8a Do you have evidence to support your deduction? ☐ Yes ☐ No

b If "Yes," is the evidence written? ☐ Yes ☐ No

SCHEDULE D (Form 1040)

Capital Gains and Losses

1999

STEPHEN R & REBECCA R CHANDLER

Part I Short-Term Capital Gains and Losses - Assets Held One Year or Less

1					
2 Enter your short-term totals		2			
3 Total short-term sales price amounts. Add column (d) of lines 1 and 2		3			
4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824				4	
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	SEE STATEMENT 12			5	21,391.
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your 1998 Capital Loss Carryover Worksheet				6	
7 Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)			▶	7	21,391.

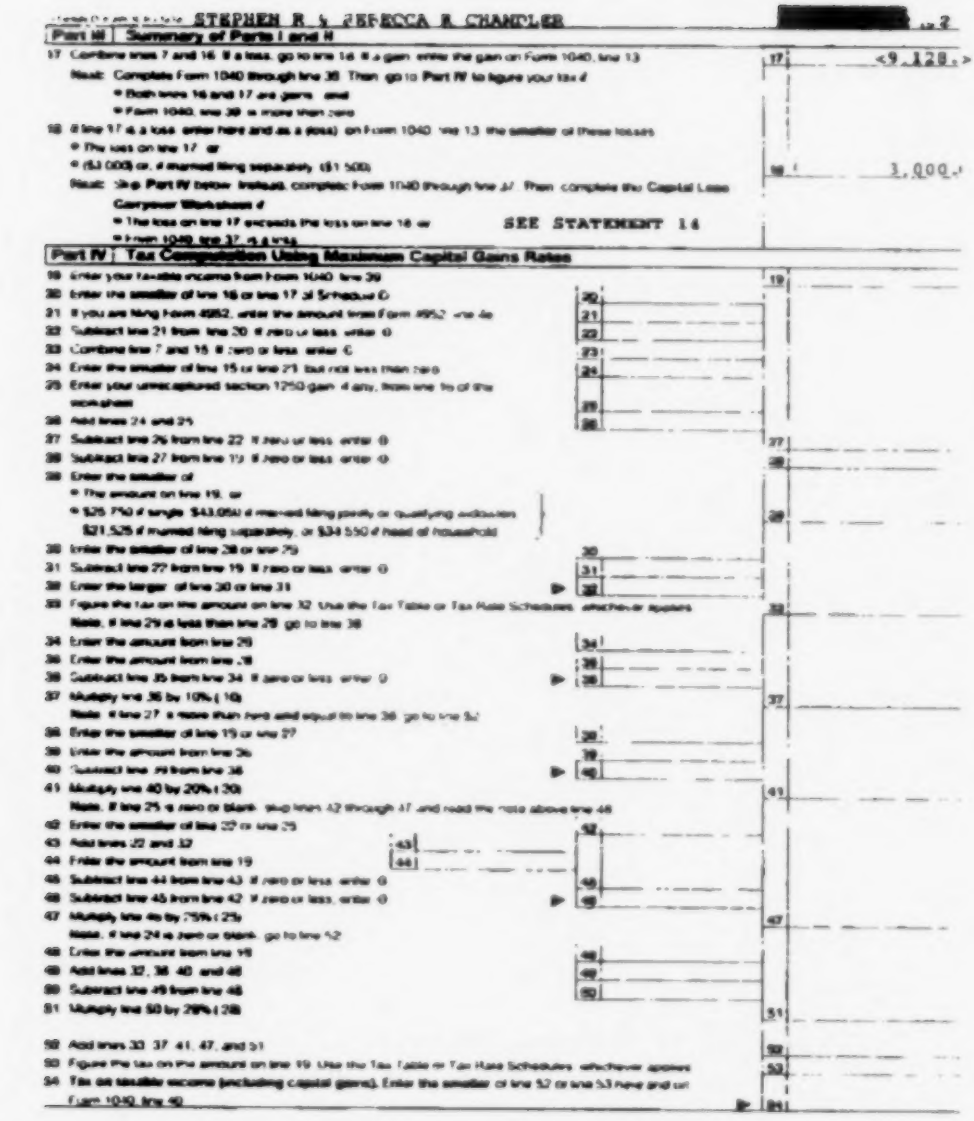
Part II Long-Term Capital Gains and Losses - Assets Held More Than One Year

9					
9 Enter your long-term totals		9			
10 Total long-term sales price amounts. Add column (d) of lines 8 and 9		10			
11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824				11	
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1	SEE STATEMENT 13			12	<30,519>
13 Capital gain distributions				13	
14 Long-term capital loss carryover. Enter in both columns (f) and (g) the amount, if any, from line 13 of your 1998 Capital Loss Carryover Worksheet				14	
15 Combine lines 9 through 14 in column (g)				15	
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f). Next: Go to Part III on page 2			▶	16	<30,519>

* 28% Rate Gain or Loss includes all "collectibles gains and losses" and up to 50% of the eligible gain on qualified small business stock.

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule D (Form 1040) 1999

DOJ-019139



STEPHEN R & REBECCA R CHANDLER [redacted] Page 2

Part III Summary of Parts I and II

17 Combine lines 7 and 16. If a loss, go to line 18. If a gain, enter the gain on Form 1040, line 13 — 17 <9,128.>

Next: Complete Form 1040 through line 38. Then go to Part IV to figure your tax if

- Both lines 16 and 17 are gains, and
- Form 1040, line 38, is more than zero

18 If line 17 is a loss, enter here and as a (loss) on Form 1040, line 13, the smaller of these losses

- The loss on line 17, or
- ($3,000) or, if married filing separately, ($1,500) — 18 1,000.

Next: Skip Part IV below. Instead, complete Form 1040 through line 37. Then complete the Capital Loss Carryover Worksheet if

- The loss on line 17 exceeds the loss on line 18, or SEE STATEMENT 14
- Form 1040, line 37, is a loss

Part IV Tax Computation Using Maximum Capital Gains Rates

19 Enter your taxable income from Form 1040, line 39 — 19

20 Enter the smaller of line 16 or line 17 of Schedule D — 20

21 If you are filing Form 4952, enter the amount from Form 4952, line 4e — 21

22 Subtract line 21 from line 20. If zero or less, enter -0- — 22

23 Combine line 7 and 15. If zero or less, enter -0- — 23

24 Enter the smaller of line 15 or line 23, but not less than zero — 24

25 Enter your unrecaptured section 1250 gain, if any, from line 11 of the worksheet — 25

26 Add lines 24 and 25 — 26

27 Subtract line 26 from line 22. If zero or less, enter -0- — 27

28 Subtract line 27 from line 19. If zero or less, enter -0- — 28

29 Enter the smaller of:

- The amount on line 19, or
- $26,750 if single; $43,050 if married filing jointly or qualifying widow(er); $21,525 if married filing separately; or $34,550 if head of household — 29

30 Enter the smaller of line 28 or line 29 — 30

31 Subtract line 27 from line 19. If zero or less, enter -0- — 31

32 Enter the larger of line 30 or line 31 — 32

33 Figure the tax on the amount on line 32. Use the Tax Table or Tax Rate Schedules, whichever applies — 33

Note. If line 29 is less than line 28, go to line 38.

34 Enter the amount from line 29 — 34

35 Enter the amount from line 28 — 35

36 Subtract line 35 from line 34. If zero or less, enter -0- — 36

37 Multiply line 36 by 10% (.10) — 37

Note. If line 27 is more than zero and equal to line 36, go to line 51.

38 Enter the smaller of line 19 or line 27 — 38

39 Enter the amount from line 36 — 39

40 Subtract line 39 from line 38 — 40

41 Multiply line 40 by 20% (.20) — 41

Note. If line 25 is zero or blank, skip lines 42 through 47, and read the note above line 48.

42 Enter the smaller of line 22 or line 25 — 42

43 Add lines 22 and 32 — 43

44 Enter the amount from line 19 — 44

45 Subtract line 44 from line 43. If zero or less, enter -0- — 45

46 Subtract line 45 from line 42. If zero or less, enter -0- — 46

47 Multiply line 46 by 25% (.25) — 47

Note. If line 24 is zero or blank, go to line 52.

48 Enter the amount from line 16 — 48

49 Add lines 32, 36, 40, and 46 — 49

50 Subtract line 49 from line 48 — 50

51 Multiply line 50 by 28% (.28) — 51

52 Add lines 33, 37, 41, 47, and 51 — 52

53 Figure the tax on the amount on line 19. Use the Tax Table or Tax Rate Schedules, whichever applies — 53

54 Tax on taxable income (including capital gains). Enter the smaller of line 52 or line 53 here and on Form 1040, line 40 — 54

DOJ-019140

STEPHEN R & REBECCA R CHANDLER

Part II Income or Loss From Partnerships and S Corporations

27	(a) Name	(b) Enter P for partnership; S for S corporation	(c) Check if foreign partnership	(d) Employer identification number	(e) Check if any amount is not at risk
A	HOME OIL & COAL CO	S		56-0546791	X
B	HOME CONCRETE & SUPPLY LLC	P		56-2136387	X
C					
D					
E					

	Passive Income and Loss		Nonpassive Income and Loss		
	(g) Passive loss allowed (attach Form 8582 if required)	(h) Passive income from Schedule K-1	(i) Nonpassive loss from Schedule K-1	(j) Section 179 expense deduction from Form 4562	(k) Nonpassive income from Schedule K-1
A					85,601.
B			618.		
C					
D					
E					
28a	Totals				85,601.
b	Totals		618.		
29	Add columns (h) and (k) of line 28a				29 85,601.
30	Add columns (g), (i), and (j) of line 28b				30 618.
31	Total partnership and S corporation income or (loss). Combine lines 29 and 30. Enter the result here and on page 1, line 17, or the appropriate line of your return.				31 84,983.

Part III Income or Loss From Estates and Trusts

32	(a) Name	(b) Employer identification number
A		
B		

	Passive Income and Loss		Nonpassive Income and Loss	
	(c) Passive deduction or loss allowed (attach Form 8582 if required)	(d) Passive income from Schedule K-1	(e) Deduction or loss from Schedule K-1	(f) Other income from Schedule K-1
A				
B				
33a	Totals			
b	Totals			
34	Add columns (d) and (f) of line 33a			34
35	Add columns (c) and (e) of line 33b			35
36	Total partner and fiduciary income or (loss). Combine lines 34 and 35. Enter the result here and on Form 1040, line 17, or the appropriate line of your return.			36

Part IV Income or Loss From Real Estate Mortgage Investment Conduits (REMICs) - Residual Holder

37	(a) Name	(b) Employer identification number	(c) Excess inclusion from Schedules Q, line 2c	(d) Taxable income (net loss) from Schedules Q, line 1b	(e) Income from Schedules Q, line 3b

38 Combine columns (d) and (e) only. Enter the result here and on Form 1040, line 17, or the appropriate line of your return. 38

Part V Summary

39	Net farm rental income or (loss) from Form 4835. Also, complete line 41 below	39	
40	Net income or (loss). Combine lines 26, 31, 36, 38, and 39. Enter the result here and on Form 1040, line 17	40	84,983.
41	Reconciliation of Farming and Fishing Income. Enter your gross farming and fishing income reported on Form 4835, line 7; Schedule K-1 (Form 1065), line 15b; Schedule K-1 (Form 1120S), line 17; and Schedule K-1 (Form 1041), line 14 (see page E-6)	41	
42	Reconciliation for Real Estate Professionals. If you were a real estate professional (see the def inition of real estate professional on page E-6), enter the net income or (loss) you reported anywhere on Form 1040 from all rental real estate activities in which you materially participated under the passive activity loss rules	42	

Schedule E (Form 1040) 1999

15190406 767285 7021 1999.05200 CHANDLER, STEPHEN R 7021___1

1999 Income from Passthroughs

HOWE OIL & COAL CO
I.D. NUMBER: 56-0546781
TYPE: S CORPORATION

ACTIVITY INFORMATION:

HOWE OIL & COAL CO

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	85,601	
SCHEDULE E ACTIVITY INCOME (LOSS)	85,601	

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST 1986 PROPERTY	1,417
ADJUSTED GAIN OR LOSS	-119,854

OTHER K-1 INFORMATION:

INTEREST - TOTAL	10,125
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	11,335
U.S. BONDS AND OBLIGATIONS	21,460
SHORT-TERM CAPITAL GAIN (LOSS)	21,302
LONG-TERM CAPITAL GAIN (LOSS)	-30,392
CONTRIBUTIONS - 50% LIMITATION	410
SECTION 1231 GAIN (LOSS)	-20,823
MEDICAL PAYMENTS PAID ON BEHALF OF 2% SHAREHOLDER	1,462
NONDEDUCTIBLE EXPENSES	725

1999 Income from Passthroughs

HOME CONCRETE & SUPPLY LLC
I.D. NUMBER: 56-2136387
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

HOME CONCRETE & SUPPLY LLC

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	-618	
SCHEDULE E ACTIVITY INCOME (LOSS)		-618

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	160
ADJUSTED GAIN OR LOSS	-500

OTHER K 1 INFORMATION:

INTEREST - TOTAL	-77
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	13
U.S. BONDS AND OBLIGATIONS	90
SHORT-TERM CAPITAL GAIN (LOSS)	89
LONG-TERM CAPITAL GAIN (LOSS)	-127
SECTION 1231 GAIN (LOSS)	-87

1999 Income from Passthroughs

SUMMARY OF K-1 INFORMATION FOR ALL PASSTHROUGHS

OTHER K-1 INFORMATION:

INTEREST - TOTAL	-10,202
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	11,348
U.S. BONDS AND OBLIGATIONS	-21,550
SHORT-TERM CAPITAL GAIN (LOSS)	21,391
LONG-TERM CAPITAL GAIN (LOSS)	-30,519
SECTION 1231 GAIN (LOSS)	-20,910
MEDICAL PAYMENTS PAID ON BEHALF OF 2% SHAREHOLDER	1,462
NONDEDUCTIBLE EXPENSES	725

DEDUCTIONS:

CONTRIBUTIONS - 50% LIMITATION	410

INVESTMENT INTEREST EXPENSE:

INVESTMENT INCOME	-10,202

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	1,577
ADJUSTED GAIN OR LOSS	-120,354

Name of person with self-employment income (as shown on Form 1040) | Social security number of person with self-employment income ▶ [redacted]

STEPHEN R CHANDLER

Section B - Long Schedule SE

Part I Self-Employment Tax

Note: If your only income subject to self-employment tax is church employee income, skip lines 1 through 4b. Enter -0- on line 4c and go to line 5a. Income from services you performed as a minister or a member of a religious order is not church employee income. See page SE-1.

A If you are a minister, member of a religious order, or Christian Science practitioner and you filed Form 4361 but you had $400 or more of other net earnings from self-employment, check here and continue with Part I ▶ ☐

1	Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a. Note: Skip this line if you use the farm optional method. See page SE-3	1	
2	Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report. Note: Skip this line if you use the nonfarm optional method. See page SE-3	SEE STATEMENT 15 2	9,000.
3	Combine lines 1 and 2	3	9,000.
4a	If line 3 is more than zero, multiply line 3 by 92.35% (.9235). Otherwise, enter amount from line 3	4a	8,312.
b	If you elected one or both of the optional methods, enter the total of lines 15 and 17 here	4b	
c	Combine lines 4a and 4b. If less than $400, do not file this schedule; you do not owe self-employment tax. Exception: If less than $400 and you had church employee income, enter -0- and continue ▶	4c	8,312.
5a	Enter your church employee income from Form W-2. Caution: See page SE-1 for definition of church employee income	5a	
b	Multiply line 5a by .9235. If less than $100, enter -0-	5b	
6	Net earnings from self-employment. Add lines 4c and 5b	6	8,312.
7	Maximum amount of combined wages and self-employment earnings subject to social security tax or the 6.2% portion of the 7.65% railroad retirement (tier 1) tax for 1999	7	72,600.00
8a	Total social security wages and tips (total of boxes 3 and 7 on Form(s) W-2) and railroad retirement (tier 1) compensation	8a 72,600.	
b	Unreported tips subject to social security tax (from Form 4137, line 9)	8b	
c	Add lines 8a and 8b	8c	72,600.
9	Subtract line 8c from line 7. If zero or less, enter -0- here and on line 10 and go to line 11	9	0.
10	Multiply the smaller of line 6 or line 9 by 12.4% (.124)	10	0.
11	Multiply line 6 by 2.9% (.029)	11	241.
12	Self-employment tax. Add lines 10 and 11. Enter here and on Form 1040, line 50	12	241.
13	Deduction for one-half of self-employment tax. Multiply line 12 by 50% (.5). Enter the result here and on Form 1040, line 27	13 121.	

Part II Optional Methods To Figure Net Earnings (See page SE-3.)

Farm Optional Method. You may use this method only if
• your gross farm income* was not more than $2,400, or
• your net farm profits* were less than $1,733.

14	Maximum income for optional methods	14 1,600.00
15	Enter the smaller of: two thirds (⅔) of gross farm income* (not less than zero) or $1,600. Also include this amount on line 4b above	15

Nonfarm Optional Method. You may use this method only if
• your net nonfarm profits* were less than $1,733 and also less than 72.189% of your gross nonfarm income,* and
• you had net earnings from self-employment of at least $400 in 2 of the prior 3 years.

Caution: You may use this method no more than five times.

16	Subtract line 15 from line 14	16
17	Enter the smaller of: two thirds (⅔) of gross nonfarm income* (not less than zero) or the amount on line 16. Also include this amount on line 4b above	17

* From Sch. F, line 11, and Sch. K-1 (Form 1065), line 15b.
* From Sch. C, line 31; Sch. C-EZ, line 3; Sch. K-1 (Form 1065), line 15a; and Sch. K-1 (Form 1065-B), box 9.

Schedule SE (Form 1999)

DOJ-019145

Form **4797** — **Sales of Business Property**
(Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2))
Attach to your tax return. See separate instructions.
1999

Name(s) shown on return

STEPHEN R & REBECCA R CHANDLER

Identifying number [redacted]

1 Enter the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20 | 1

Part I **Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft - Property Held More Than 1 Year**

(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) Gain or (loss) Subtract (f) from the sum of (d) and (e)
2						
HOME OIL & COAL CO						<20,823.>
HOME CONCRETE & SUPPLY LLC						<87.>

3 Gain, if any, from Form 4684, line 39	3	
4 Section 1231 gain from installment sales from Form 6252, line 26 or 37	4	
5 Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5	
6 Gain, if any, from line 32, from other than casualty or theft	6	
7 Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows: Partnerships (except electing large partnerships). Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 9. Skip lines 8, 9, 11, and 12 below. S corporations. Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax. All others. If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	7	<20,910.>
8 Nonrecaptured net section 1231 losses from prior years **SEE STATEMENT 16**	8	
9 Subtract line 8 from line 7. If zero or less, enter 0. Then enter on the appropriate line as follows: S corporations. Enter any gain from line 9 on Schedule D of Form 1120S, line 14, and skip lines 11 and 12 below. All others. If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D	9	

Part II **Ordinary Gains and Losses**

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

11 Loss, if any, from line 7	11	<20,910.>
12 Gain, if any, from line 7, or amount from line 8, if applicable	12	
13 Gain, if any, from line 31	13	
14 Net gain or (loss) from Form 4684, lines 31 and 38a	14	
15 Ordinary gain from installment sales from Form 6252, line 25 or 36	15	
16 Ordinary gain or (loss) from like-kind exchanges from Form 8824	16	
17 Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations	17	
18 Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18	<20,910.>
a For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.		
b For individual returns: (1) If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)."	18b(1)	
(2) Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)	<20,910.>

LHA For Paperwork Reduction Act Notice, see separate instructions. Form 4797 (1999)

15190406 767285 7021 1999.05200 CHANDLER, STEPHEN R 7021 1

Form 4797 (1999) STEPHEN R & REBECCA R CHANDLER [redacted] Page 2

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255

		(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:			
A			
B			
C			
D			

These columns relate to the properties on lines 19A through 19D.		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20				
21 Cost or other basis plus expense of sale	21				
22 Depreciation (or depletion) allowed or allowable	22				
23 Adjusted basis. Subtract line 22 from line 21	23				
24 Total gain. Subtract line 23 from line 20	24				
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a				
b Enter the smaller of line 24 or 25a	25b				
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines, and other mineral deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under sec. 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation	34		
35 Recapture amount. Subtract line 34 from line 33	35		

Form 4797 (1999)

15190406 767285 7021 1999.05200 CHANDLER, STEPHEN R 7021 1

Form 8283 — Noncash Charitable Contributions

▶ Attach to your tax return if you claimed a total deduction of over $500 for all contributed property

Name(s) shown on your income tax return — Identifying number

STEPHEN R & REBECCA R CHANDLER — [redacted]

Note. Figure the amount of your contribution deduction before completing this form. See your tax return instructions.

Section A. - List in this section only items (or groups of similar items) for which you claimed a deduction of $5,000 or less. Also, list certain publicly traded securities even if the deduction is over $5,000 (see instructions).

Part I — Information on Donated Property - If you need more space, attach a statement.

	(a) Name and address of the donee organization	(b) Description of donated property
A	GOODWILL INDUSTRIES WINSTON SALEM, NC	CLOTHING & MISC ITEMS
B	HABITAT GENERAL STORE SALISBURY, NC 28145	MISC PERSONAL ITEMS
C	COBURN MEMORIAL UMC BOY SCOUTS SALISBURY, NC 28144	14' ODAY SAILBOAT & TRAILER
D		
E		

Note. If the amount you claimed as a deduction for an item is $500 or less, you do not have to complete columns (c), (d), and (e).

	(c) Date of the contribution	(d) How acquired by donor	(e) Donor's cost or adjusted basis	(f) Fair market value	(g) Method used to determine the fair market value
A	09/17/99	PURCHASE	2,000.	525.	THRIFT SHOP VALUE
B	11/16/99	PURCHASE	8,000.	2,000.	THRIFT SHOP VALUE
C	08/12/99	PURCHASE	8,000.	1,600.	COMPARABLE SALES
D					
E					

Part II — Other Information - Complete line 2 if you gave less than an entire interest in property listed in Part I. Complete line 3 if conditions were attached to a contribution listed in Part I.

2 If, during the year, you contributed less than the entire interest in the property, complete lines a - e.

a Enter the letter from Part I that identifies the property ▶ _____ If Part II applies to more than one property, attach a separate statement.

b Total amount claimed as a deduction for the property listed in Part I: (1) For this tax year ▶ _____ (2) For any prior tax years ▶ _____

c Name and address of each organization to which any such contribution was made in a prior year (complete only if different than the donee organization above)

d For tangible property, enter the place where the property is located or kept ▶ _____

e Name of any person, other than the donee organization, having actual possession of the property ▶ _____

3 If conditions were attached to any contribution listed in Part I, answer questions a - c and attach the required statement. — Yes / No

a Is there a restriction, either temporary or permanent, on the donee's right to use or dispose of the donated property?

b Did you give to anyone (other than the donee organization or another conservation partner participating with the donee organization or cooperating further along) the right to the income from the donated property or to the possession of the property, or a right to vote donated securities, to acquire the property by purchase or other way, or to designate the person having such income, possession, or right to acquire?

c Is there a restriction limiting the donated property to a particular use?

LHA For Paperwork Reduction Act Notice, see separate instructions. — Form 8283 (Rev. 10-98)

DOJ-019148

STEPHEN R & REBECCA R CHANDLER [redacted]

FOOTNOTES STATEMENT 1

DURING THE YEAR THE PROCEEDS OF A SHORT SALE NOT CLOSED BY THE TAXPAYER DURING THIS TAX YEAR WERE RECEIVED.

DOJ-019149

STEPHEN R & REBECCA R CHANDLER [redacted]

FORM 1040	PENSIONS AND ANNUITIES	STATEMENT 2
HOME OIL & COAL 401K PROFIT SHARING TRUST		
AMOUNT RECEIVED THIS YEAR	101,714.	
NONTAXABLE AMOUNT (ROLLOVER)	101,714.	
CAPITAL GAIN DISTRIBUTION REPORTED ON SCH D		
AMOUNT INCLUDED IN FORM 1040, LINE 16B		0.
TOTAL INCLUDED IN FORM 1040, LINE 16B		0.

STEPHEN R & REBECCA R CHANDLER [redacted]

FORM 1040 PERSONAL EXEMPTION WORKSHEET STATEMENT 3

1.	IS THE AMOUNT ON FORM 1040, LINE 36, MORE THAN THE AMOUNT SHOWN ON LINE 4 BELOW FOR YOUR FILING STATUS? NO. STOP. MULTIPLY $2,750 BY THE TOTAL NUMBER OF EXEMPTIONS CLAIMED ON FORM 1040, LINE 6D, AND ENTER THE RESULT ON LINE 38. YES. GO TO LINE 2.			
2.	MULTIPLY $2,750 BY THE TOTAL NUMBER OF EXEMPTIONS CLAIMED ON FORM 1040, LINE 6D			5,500.
3.	ENTER THE AMOUNT FROM FORM 1040, LINE 36 . .		283,618.	
4.	ENTER THE AMOUNT FOR YOUR FILING STATUS . .		189,950.	
	MARRIED FILING SEPARATE	$ 94,975		
	SINGLE	$126,600		
	HEAD OF HOUSEHOLD	$158,300		
	MARRIED FILING JOINT OR WIDOW(ER)	$189,950		
5.	SUBTRACT LINE 4 FROM LINE 3		93,668.	
	IF LINE 5 IS MORE THAN $122,500 ($61,250 IF MARRIED FILING SEPARATE) ENTER ZERO ON FORM 1040, LINE 38.			
6.	DIVIDE LINE 5 BY $2,500 ($1,250 IF MFS) . .		38.	
7.	MULTIPLY LINE 6 BY 2% (.02) AND ENTER THE RESULT AS A DECIMAL		0.76	
8.	MULTIPLY LINE 2 BY LINE 7			4,180.
9.	SUBTRACT LINE 8 FROM LINE 2. TOTAL TO FORM 1040, LINE 38.			1,320.

DOJ-019151

STEPHEN R & REBECCA R CHANDLER [redacted]

FORM 1040 — SEP DEDUCTION — STATEMENT 4

STEPHEN R CHANDLER

1.	PLAN CONTRIBUTION RATE OR SELF-EMPLOYED PERSON'S RATE	.130435
2.	NET EARNINGS FROM SCHEDULE C, SCHEDULE F, OR SCHEDULE K-1	9,000.
3.	DEDUCTION FOR SELF-EMPLOYMENT TAX FROM 1040, LINE 27	121.
4.	SUBTRACT LINE 3 FROM LINE 2	8,879.
5.	MULTIPLY LINE 4 TIMES LINE 1	1,158.
6.	MULTIPLY $160,000 BY YOUR PLAN CONTRIBUTION RATE. ENTER THE RESULT BUT NOT MORE THAN $30,000	24,000.
7.	ENTER THE SMALLER OF LINE 5 OR LINE 6 HERE AND ON LINE 29 FORM 1040	1,158.

FORM 1040 — WAGES RECEIVED AND TAXES WITHHELD — STATEMENT 5

T S	EMPLOYER'S NAME	AMOUNT PAID	FEDERAL TAX WITHHELD	STATE TAX WITHHELD	CITY SDI TAX W/H	FICA TAX	MEDICARE TAX
T	HOWE OIL & COAL, SALISBURY, NC	151,749.	44,075.	10,865.		4,501.	2,345.
T	CENTRAL CONCRETE	32,511.	6,105.	2,289.		2,016.	471.
TOTALS		184,260.	50,180.	13,154.		6,517.	2,816.

DOJ-019152

STEPHEN R & REBECCA R CHANDLER [redacted]

FORM 1040 EXCESS SOCIAL SECURITY TAX WORKSHEET STATEMENT 6

	TAXPAYER	SPOUSE
1. ADD ALL SOCIAL SECURITY TAX WITHHELD BUT NOT MORE THAN $4,501.20 FOR EACH EMPLOYER (THIS TAX SHOULD BE SHOWN IN BOX 4 OF YOUR W-2 FORMS). ENTER THE TOTAL HERE	6,517.	
2. ENTER ANY UNCOLLECTED SOCIAL SECURITY TAX ON TIPS OR GROUP-TERM LIFE INSURANCE INCLUDED IN THE TOTAL ON FORM 1040, LINE 56		
3. ADD LINES 1 AND 2	6,517.	
4. SOCIAL SECURITY TAX LIMIT	4,501.	
5. SUBTRACT LINE 4 FROM LINE 3. EXCESS SOCIAL SECURITY TAX INCLUDED IN FORM 1040, LINE 62	2,016.	

SCHEDULE A STATE AND LOCAL INCOME TAXES STATEMENT 7

DESCRIPTION	AMOUNT
HOME OIL & COAL, SALISBURY, NC	10,865.
CENTRAL CONCRETE	2,289.
NORTH CAROLINA ESTIMATE PAYMENTS	22,640.
NORTH CAROLINA PRIOR YEAR BALANCE DUE AND EXTENSION PAYMENTS	583.
TOTAL TO SCHEDULE A, LINE 5	36,377.

SCHEDULE A CASH CONTRIBUTIONS STATEMENT 8

DESCRIPTION	AMOUNT 50% LIMIT	AMOUNT 30% LIMIT
MISCELLANEOUS	787.	
FROM K-1 - HOME OIL & COAL CO	410.	
SUBTOTALS	1,197.	
TOTAL TO SCHEDULE A, LINE 15		1,197.

DOJ-019153

STEPHEN R & REBECCA R CHANDLER [redacted]

SCHEDULE A MEDICAL AND DENTAL EXPENSES STATEMENT 9

DESCRIPTION	AMOUNT
PRESCRIPTION MEDICINES AND DRUGS	450.
DOCTORS, DENTISTS, ETC.	4,758.
EYEGLASSES AND CONTACTS	381.
MEDICAL PAYMENTS PAID ON BEHALF 2% SHAREHOLDER FROM K-1 - HOWE OIL & COAL CO	1,462.
TOTAL TO SCHEDULE A, LINE 1	7,051.

STEPHEN R & REBECCA R CHANDLER [redacted]

SCHEDULE A	ITEMIZED DEDUCTIONS WORKSHEET		STATEMENT 10
1.	ADD THE AMOUNTS ON SCHEDULE A, LINES 4, 9, 14, 18, 19, 26, AND 27		48,525.
2.	ADD THE AMOUNTS ON SCHEDULE A, LINES 4, 13, AND 19, PLUS ANY GAMBLING AND CASUALTY OR THEFT LOSSES INCLUDED ON LINE 27		0.
3.	IS THE AMOUNT ON LINE 2 LESS THAN THE AMOUNT ON LINE 1? IF NO, YOUR DEDUCTION IS NOT LIMITED. ENTER THE AMOUNT FROM LINE 1 ABOVE ON SCHEDULE A, LINE 28. IF YES, SUBTRACT LINE 2 FROM LINE 1		48,525.
4.	MULTIPLY LINE 3 ABOVE BY 80% (.80)	38,820.	
5.	ENTER THE AMOUNT FROM FORM 1040, LINE 34.	283,618.	
6.	ENTER: $126,600 IF SINGLE, MARRIED FILING JOINTLY, HEAD OF HOUSEHOLD, OR QUALIFYING WIDOW(ER); $63,300 IF MARRIED FILING SEPARATELY	126,600.	
7.	IS THE AMOUNT ON LINE 6 LESS THAN THE AMOUNT ON LINE 5? IF NO, YOUR DEDUCTION IS NOT LIMITED. ENTER THE AMOUNT FROM LINE 1 ABOVE ON SCHEDULE A, LINE 28. IF YES, SUBTRACT LINE 6 FROM LINE 5	157,018.	
8.	MULTIPLY LINE 7 ABOVE BY 3% (.03)	4,711.	
9.	ENTER THE SMALLER OF LINE 4 OR LINE 8		4,711.
10.	TOTAL ITEMIZED DEDUCTIONS. SUBTRACT LINE 9 FROM LINE 1. ENTER THE RESULT HERE AND ON SCHEDULE A, LINE 28		43,814.

SCHEDULE C-EZ	GROSS RECEIPTS	STATEMENT 11
DESCRIPTION		AMOUNT
HOME OIL & COAL DIRECTOR FEES		9,000.
TOTAL TO SCHEDULE C EZ, LINE 1		9,000.

STEPHEN R & REBECCA R CHANDLER [redacted]

SCHEDULE D — NET SHORT-TERM GAIN OR LOSS FROM PARTNERSHIPS, S CORPORATIONS, AND FIDUCIARIES — STATEMENT 12

DESCRIPTION OF ACTIVITY	GAIN OR LOSS
[redacted] OIL & COAL CO	21,302.
[redacted] CONCRETE & SUPPLY LLC	89.
TOTAL TO SCHEDULE D, PART I, LINE 5	21,391.

SCHEDULE D — NET LONG-TERM GAIN OR LOSS FROM PARTNERSHIPS, S CORPORATIONS, AND FIDUCIARIES — STATEMENT 13

DESCRIPTION OF ACTIVITY	GAIN OR LOSS	28% GAIN
[redacted] OIL & COAL CO	<30,392.>	
[redacted] CONCRETE & SUPPLY LLC	<127.>	
TOTAL TO SCHEDULE D, PART II, LINE 12	<30,519.>	

Case 7:06-cv-00181-FL Document 26-6 Filed 04/19/07 Page 23 of 28

DOJ-019156

STEPHEN R & REBECCA R CHANDLER [redacted]

SCHEDULE D	CAPITAL LOSS CARRYOVER	STATEMENT 14
1. ENTER THE AMOUNT FROM FORM 1040, LINE 37		239,804.
2. ENTER THE LOSS FROM SCHEDULE D, LINE 16, AS A POSITIVE AMOUNT.		3,000.
3. COMBINE LINES 1 AND 2. IF ZERO OR LESS, ENTER -0-		242,804.
4. ENTER THE SMALLER OF LINE 2 OR LINE 3		3,000.
5. ENTER THE LOSS FROM SCHEDULE D, LINE 7, AS A POSITIVE AMOUNT		
6. ENTER THE GAIN, IF ANY, FROM SCHEDULE D, LINE 15		
7. ADD LINES 4 AND 6		
8. SHORT TERM CAPITAL LOSS CARRYOVER TO 2008. SUBTRACT LINE 7 FROM LINE 5. IF ZERO OR LESS, ENTER -0-		
9. ENTER THE LOSS FROM SCHEDULE D, LINE 15, AS A POSITIVE AMOUNT.		30,519.
10. ENTER THE GAIN, IF ANY, FROM SCHEDULE D, LINE 7	21,391.	
11. SUBTRACT LINE 5 FROM LINE 4. IF ZERO OR LESS, ENTER -0-	3,000.	
12. ADD LINES 10 AND 11		24,391.
13. LONG-TERM CAPITAL LOSS CARRYOVER TO 2008. SUBTRACT LINE 12 FROM LINE 9. IF ZERO OR LESS, ENTER -0-		6,128.

SCHEDULE SE	NON-FARM INCOME	STATEMENT 15
DESCRIPTION		AMOUNT
FROM SCHEDULE C		9,000.
TOTAL TO SCHEDULE SE, LINE 2		9,000.

STEPHEN R & REBECCA N CHANDLER [redacted]

FORM 4797 NONRECAPTURED NET SECTION 1231 LOSSES FROM PRIOR YEARS STATEMENT 16

TAX YEAR	SECTION 1231 LOSSES	SECTION 1231 LOSSES RECAPTURED	NONRECAPTURED SECTION 1231 LOSSES
1994	159.	159.	
1995	23.	14.	9.
1996			
1997			
1998			
TOTAL TO FORM 4797, LINE 8	182.	173.	9.

Transferor's Statement under
Reg 1.351-3(a)
Stephen R. Chandler
SSN [redacted]
From 1948, Tax Year Ending 12/31/1999

1. Description of property transferred.
Property transferred by Stephen R. Chandler June 14, 1999

Property
.3387% interest in Home Concrete Supply LLC EIN 56-2136387

2. Cost or basis in hands of transferor as of date of transfer
Stephen R. Chandler $ 1,138,398.13

3. i. Total issued and outstanding capital stock immediately prior to the exchange 5,300

ii. Total issued and outstanding capital stock immediately after the exchange 5,300

iii. Stock issued in the exchange None

Shares owned by transferor immediately prior to and after the exchange:

Stephen R. Chandler 1,000

iii. Fair market value of stock issued to transferor. Not applicable

4. i. Principal amount and terms of all securities outstanding immediately prior to and immediately after the exchange: Not applicable

ii. Principal amount and terms of all securities issued to transferors in the exchange and the transferor's holdings of securities immediately prior to and immediately after the exchange: Not applicable

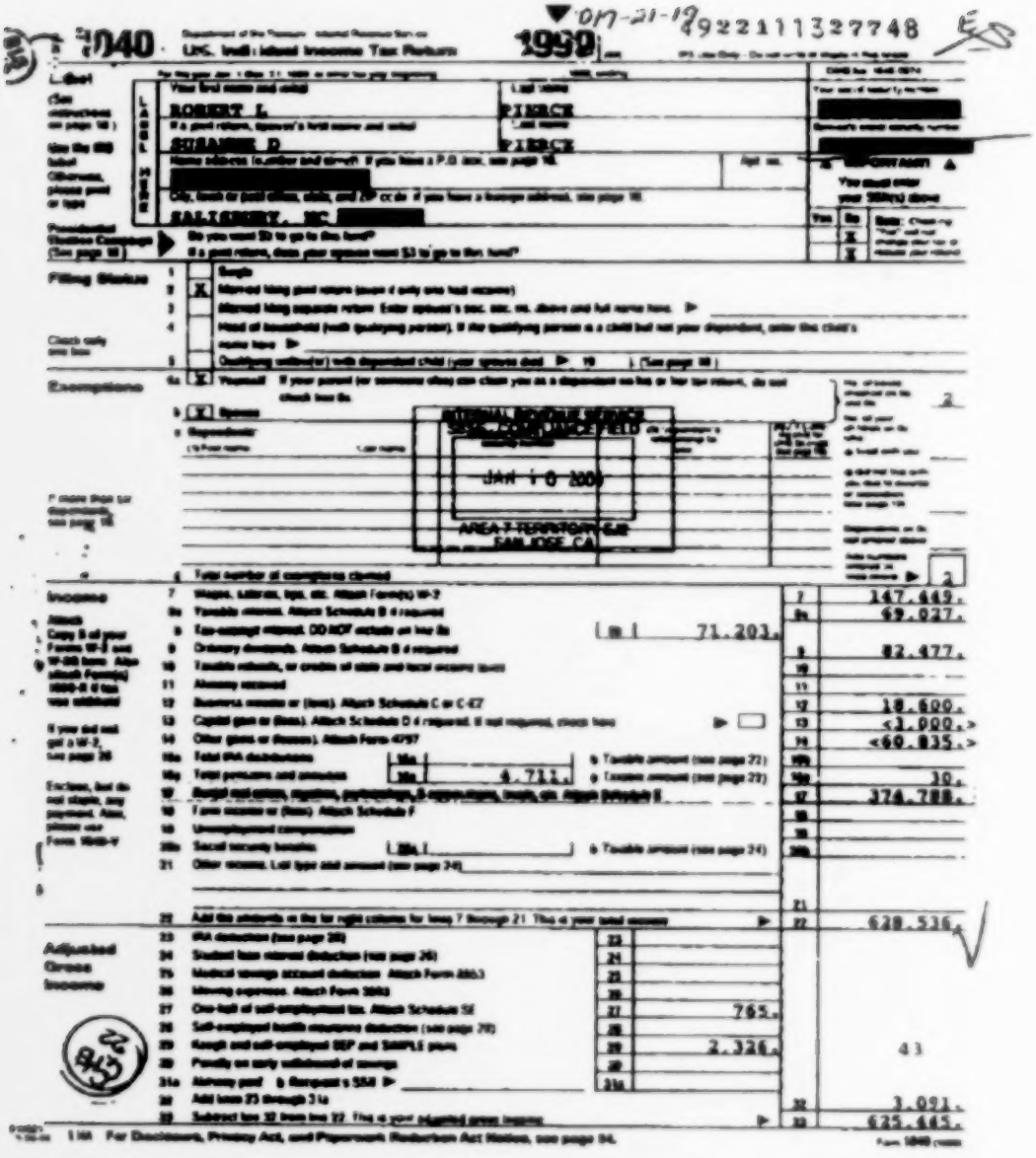
iii. Fair market value of securities issued to transferor: Not applicable

5. Amount of money passed to transferors: None

6. Other property which was passed to transferors: None

7. Liabilities assumed by the controlled corporation in the exchange: None

Case 7:06-cv-00181-FL Document 22 Filed 04/19/2007 Page 1 of 2
GOVERNMENT EXHIBIT 29
EXHIBIT A



Form 1040 U.S. Individual Income Tax Return 1999

▼ 09-21-12 9221113277 48

Label: ROBERT L PIERCE; SUSANNE D PIERCE; SALISBURY, NC [redacted]

Filing Status: X Married filing joint return

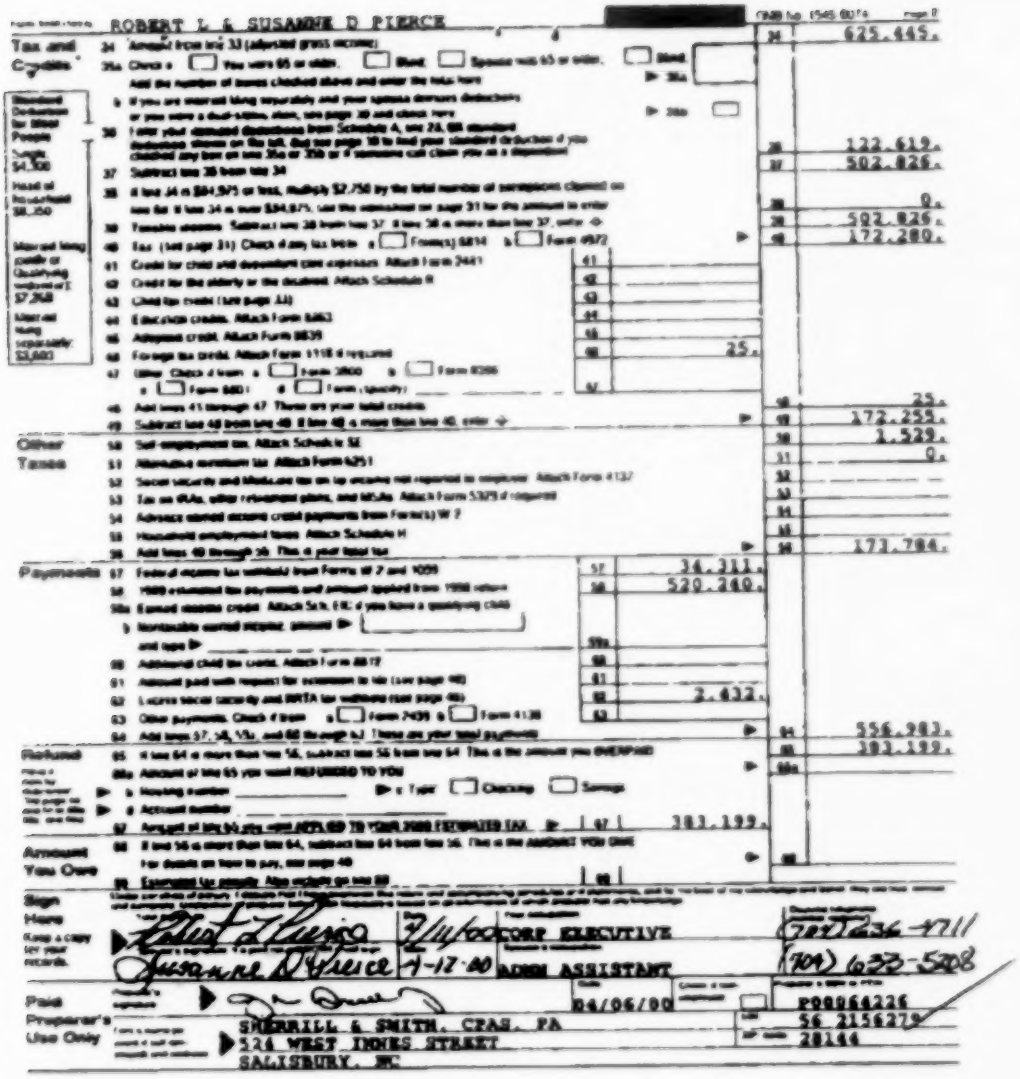
Exemptions: 2

IRS stamp: JAN 10 2000 AREA 7-TERRITORY 6-IR SAN JOSE CA

7	Wages, salaries, tips, etc. Attach Form(s) W-2	147,449.
8a	Taxable interest. Attach Schedule B if required	69,027.
b	Tax-exempt interest. DO NOT include on line 8a	71,201.
9	Ordinary dividends. Attach Schedule B if required	82,477.
10	Taxable refunds, or credits of state and local income taxes	
11	Alimony received	
12	Business income or (loss). Attach Schedule C or C-EZ	18,600.
13	Capital gain or (loss). Attach Schedule D if required. If not required, check here	<1,000.>
14	Other gains or (losses). Attach Form 4797	<60,835.>
15a	Total IRA distributions 15a	b Taxable amount
16a	Total pensions and annuities 16a 4,711.	b Taxable amount 10.
17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E	374,788.
18	Farm income or (loss). Attach Schedule F	
19	Unemployment compensation	
20a	Social security benefits 20a	b Taxable amount
21	Other income. List type and amount	
22	Add the amounts in the far right column for lines 7 through 21. This is your total income	628,536.
23	IRA deduction	
24	Student loan interest deduction	
25	Medical savings account deduction. Attach Form 8853	
26	Moving expenses. Attach Form 3903	
27	One-half of self-employment tax. Attach Schedule SE	765.
28	Self-employed health insurance deduction	
29	Keogh and self-employed SEP and SIMPLE plans	2,326.
30	Penalty on early withdrawal of savings	
31a	Alimony paid b Recipient's SSN	
32	Add lines 23 through 31a	3,091.
33	Subtract line 32 from line 22. This is your adjusted gross income	625,445.

Adjusted Gross Income

43



ROBERT L & SUSANNE D PIERCE [redacted]

34	Amount from line 33 (adjusted gross income)		625,445.
36	Subtract line 35 from line 34		122,619.
37	Subtract line 36 from line 34		502,826.
38	If line 34 is $84,975 or less, multiply $2,750 by the total number of exemptions claimed on line 6d. If line 34 is more than $84,975, use the worksheet on page 31 for the amount to enter.		0.
39	Taxable income. Subtract line 38 from line 37. If line 38 is more than line 37, enter -0-		502,826.
40	Tax (see page 31). Check if any tax is from a Form(s) 8814 b Form 4972		172,280.
41	Credit for child and dependent care expenses. Attach Form 2441	41	
42	Credit for the elderly or the disabled. Attach Schedule R	42	
43	Child tax credit (see page 32)	43	
44	Education credits. Attach Form 8863	44	
45	Adoption credit. Attach Form 8839	45	
46	Foreign tax credit. Attach Form 1116 if required	46	25.
47	Other credits. Check if from a Form 3800 b Form 8396 c Form 8801 d Form (specify)	47	
48	Add lines 41 through 47. These are your total credits	48	25.
49	Subtract line 48 from line 40. If line 48 is more than line 40, enter -0-	49	172,255.
50	Self-employment tax. Attach Schedule SE	50	1,529.
51	Alternative minimum tax. Attach Form 6251	51	0.
52	Social security and Medicare tax on tip income not reported to employer. Attach Form 4137	52	
53	Tax on IRAs, other retirement plans, and MSAs. Attach Form 5329 if required	53	
54	Advance earned income credit payments from Form(s) W-2	54	
55	Household employment taxes. Attach Schedule H	55	
56	Add lines 49 through 55. This is your total tax	56	173,784.
57	Federal income tax withheld from Forms W-2 and 1099	57	34,311.
58	1998 estimated tax payments and amount applied from 1998 return	58	520,240.
59a	Earned income credit. Attach Sch. EIC if you have a qualifying child	59a	
b	Nontaxable earned income: amount ▶ and type ▶		
60	Additional child tax credit. Attach Form 8812	60	
61	Amount paid with request for extension to file (see page 48)	61	
62	Excess social security and RRTA tax withheld (see page 48)	62	2,432.
63	Other payments. Check if from a Form 2439 b Form 4136	63	
64	Add lines 57, 58, 59a, and 60 through 63. These are your total payments	64	556,983.
65	If line 64 is more than line 56, subtract line 56 from line 64. This is the amount you OVERPAID	65	383,199.
66a	Amount of line 65 you want REFUNDED TO YOU	66a	
b	Routing number ▶ c Type ▶ Checking Savings		
d	Account number ▶		
67	Amount of line 65 you want APPLIED TO YOUR 2000 ESTIMATED TAX ▶	67	383,199.
68	If line 56 is more than line 64, subtract line 64 from line 56. This is the AMOUNT YOU OWE	68	
69	Estimated tax penalty. Also include on line 68	69	

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Sign Here	Your signature: Robert L Pierce	Date: 4-17-00	Your occupation: CORP EXECUTIVE	Daytime phone number: (704) 636-4711
Keep a copy for your records.	Spouse's signature: Susanne D Pierce	4-17-00	ADMIN ASSISTANT	(704) 633-5308
Paid Preparer's Use Only	Preparer's signature:	Date: 04/06/00	Check if self-employed:	Preparer's SSN or PTIN: P00864226
	Firm's name: SHERRILL & SMITH, CPAS, PA			Firm's EIN: 56 2156279
	Firm's address: 524 WEST INNES STREET SALISBURY, NC			ZIP code: 28144

SCHEDULES A&B (Form 1040)

Schedule A - Itemized Deductions

(Schedule B is on page 2)

1999

ROBERT L & SUSANNE D PIERCE

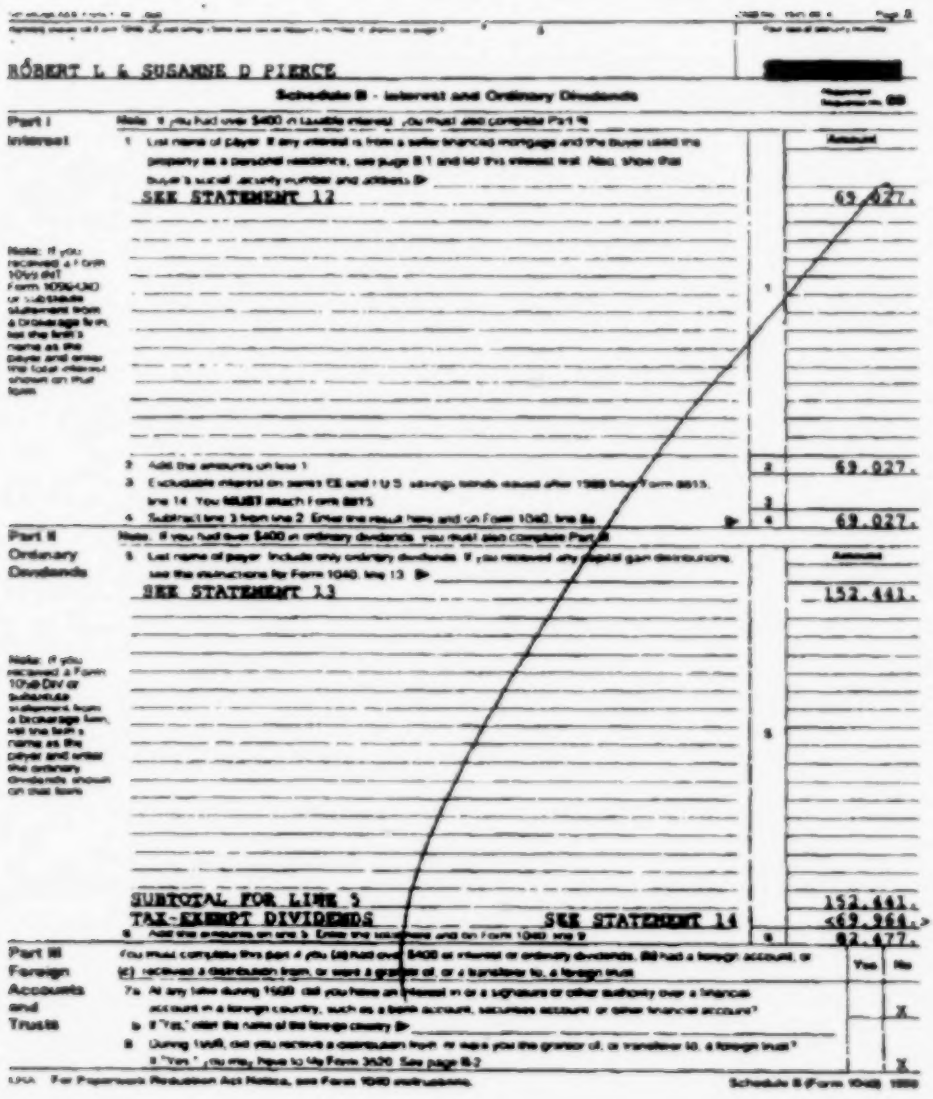
Medical and Dental Expenses	1	Medical and dental expenses (see page A-1) SEE STATEMENT 10	1	1,462.	
	2	Enter amount from Form 1040, line 34 [2] 625,445.			
	3	Multiply line 2 above by 7.5% (.075)	3	46,908.	
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter 0			4 0.
Taxes You Paid (See page A-2)	5	State and local income taxes SEE STATEMENT 8	5	118,130.	
	6	Real estate taxes (see page A-2)	6	4,053.	
	7	Personal property taxes	7	1,120.	
	8	Other taxes. List type and amount	8		
	9	Add lines 5 through 8			9 123,323.
Interest You Paid (See page A-3) Note: Personal interest is not deductible	10	Home mortgage interest and points reported to you on Form 1098	10		
	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see page A-3 and show that person's name, identifying no., and address NATIONS BANK (1/3), SALISBURY, NC	11	117.	
	12	Points not reported to you on Form 1098. (See page A-3)	12		
	13	Investment interest. Attach Form 4952 if required. (See page A-3)	13		
	14	Add lines 10 through 13			14 117.
Gifts to Charity If you made a gift and got a benefit for it, see page A-4.	15	Gifts by cash or check. If you made any gift of $250 or more, see page A-4 SEE STATEMENT 9	15	3,190.	
	16	Other than by cash or check. If any gift of $250 or more, see page A-4. You MUST attach Form 8283 if over $500	16	10,954.	
	17	Carryover from prior year	17		
	18	Add lines 15 through 17			18 14,144.
Casualty and Theft Losses	19	Casualty or theft loss(es). Attach Form 4684. (See page A-5.)			19
Job Expenses and Most Other Miscellaneous Deductions (See page A-5 for expenses to deduct here.)	20	Unreimbursed employee expenses - job travel, union dues, job education, etc. You MUST attach Form 2106 or 2106-EZ if required. (See page A-5.)	20		
	21	Tax preparation fees	21		
	22	Other expenses - investment, safe deposit box, etc. List type and amount INVESTMENT EXPENSES-RO BUCK 55. INVESTMENT CLUB FROM X-1 - RO-BUCK MUTUAL 1. INVESTMENT CLUB	22	56.	
	23	Add lines 20 through 22	23	56.	
	24	Enter amount from Form 1040, line 34 [24] 625,445.			
	25	Multiply line 24 above by 2% (.02)	25	12,509.	
	26	Subtract line 25 from line 23. If line 25 is more than line 23, enter 0			26 0.
Other Miscellaneous Deductions	27	Other - from list on page A-6. List type and amount			27
Total Itemized Deductions	28	Is Form 1040, line 34, over $126,600 (over $63,300 if married filing separately)? STMT 11 ☐ NO. Your deduction is not limited. Add the amounts in the far right column for lines 4 through 27. Also, enter on Form 1040, line 36 ☒ YES. Your deduction may be limited. See page A-6 for the amount to enter			▶ 28 122,619.

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule A (Form 1040) 1999

6

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020 1

DOJ-018212



ROBERT L & SUSANNE D PIERCE [redacted]

Schedule B - Interest and Ordinary Dividends

Part I Interest

1 List name of payer. If any interest is from a seller-financed mortgage and the buyer used the property as a personal residence, see page B-1 and list this interest first. Also, show that buyer's social security number and address ▶

SEE STATEMENT 12 — 69,027.

Note: If you received a Form 1099-INT, Form 1099-OID or substitute statement from a brokerage firm, list the firm's name as the payer and enter the total interest shown on that form.

1 —

2 Add the amounts on line 1 — 2 — 69,027.

3 Excludable interest on series EE and I U.S. savings bonds issued after 1989 from Form 8815, line 14. You MUST attach Form 8815 — 3 —

4 Subtract line 3 from line 2. Enter the result here and on Form 1040, line 8a ▶ — 4 — 69,027.

Part II Ordinary Dividends

Note: If you had over $400 in ordinary dividends, you must also complete Part III.

5 List name of payer. Include only ordinary dividends. If you received any capital gain distributions, see the instructions for Form 1040, line 13 ▶

SEE STATEMENT 13 — 152,441.

Note: If you received a Form 1099-DIV or substitute statement from a brokerage firm, list the firm's name as the payer and enter the ordinary dividends shown on that form.

5 —

SUBTOTAL FOR LINE 5 — 152,441.

TAX-EXEMPT DIVIDENDS — SEE STATEMENT 14 — <69,964.>

6 Add the amounts on line 5. Enter the total here and on Form 1040, line 9 — 6 — 82,477.

Part III Foreign Accounts and Trusts

You must complete this part if you (a) had over $400 of interest or ordinary dividends; (b) had a foreign account; or (c) received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

	Yes	No
7a At any time during 1999, did you have an interest in or a signature or other authority over a financial account in a foreign country, such as a bank account, securities account, or other financial account?		X
b If "Yes," enter the name of the foreign country ▶		
8 During 1999, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust? If "Yes," you may have to file Form 3520. See page B-2		X

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule B (Form 1040) 1999

SCHEDULE C-EZ (Form 1040)

Department of the Treasury Internal Revenue Service (99)

Net Profit From Business

(Sole Proprietorship)

▶ Partnerships, joint ventures, etc., must file Form 1065 or 1065-B

▶ Attach to Form 1040 or Form 1041 ▶ See instructions

OMB No. 1545-0074

1999

Attachment Sequence No. 09A

Name of proprietor

ROBERT L PIERCE

Social security number (SSN)

[redacted]

Part I General Information

You May Use Schedule C-EZ Instead of Schedule C Only If You:

- Had business expenses of $2,500 or less.
- Use the cash method of accounting.
- Did not have an inventory of any items during the year.
- Did not have a net loss from your business.
- Had only one business as a sole proprietor.

And You:

- Had no employees during the year.
- Are not required to file Form 4562, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-3 to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year passive activity losses from this business.

A Principal business or profession, including product or service

DIRECTOR PERS

B Enter code from pages C-9 & 10

▶ 999999

C Business name. If no separate business name, leave blank.

ROBERT PIERCE DIRECTOR

D Employer ID number (EIN), if any

E Business address (including suite or room no.) Address not required if same as on Form 1040, page 1

310 BETHEL DRIVE

City, town or post office, state, and ZIP code

SALISBURY, NC 28144

Part II Figure Your Net Profit

1 Gross receipts. Caution: If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see Statutory Employees in the instructions for Schedule C, line 1, on page C-3 and check here ▶ ☐ SEE STATEMENT 15	1	9,600.
2 Total expenses. If more than $2,500, you must use Schedule C. See instructions.	2	0.
3 Net profit. Subtract line 2 from line 1. If less than zero, you must use Schedule C. Enter on Form 1040, line 12, and also on Schedule SE, line 2. (Statutory employees do not report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)	3	9,600.

Part III Information on Your Vehicle. Complete this part ONLY if you are claiming car or truck expenses on line 2.

4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ __/__/__

5 Of the total number of miles you drove your vehicle during 1999, enter the number of miles you used your vehicle for:

a Business _____ b Commuting _____ c Other _____

6 Do you (or your spouse) have another vehicle available for personal use?	☐ Yes	☐ No
7 Was your vehicle available for use during off-duty hours?	☐ Yes	☐ No
8a Do you have evidence to support your deduction?	☐ Yes	☐ No
b If "Yes," is the evidence written?	☐ Yes	☐ No

3

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule C-EZ (Form 1040) 1999

8

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020___1

SCHEDULE C-EZ (Form 1040)

Net Profit From Business

(Sole Proprietorship)

▶ Partnerships, joint ventures, etc., must file Form 1065 or 1065-B.
▶ Attach to Form 1040 or Form 1041. ▶ See instructions.

1999

Name of proprietor

SUSANNE D PIERCE

Social security number (SSN)

[redacted]

Part I General Information

You May Use Schedule C-EZ Instead of Schedule C Only If You:

- Had business expenses of $2,500 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not deduct a net loss from your business.
- Had only one business as a sole proprietor.

And You:

- Had no employees during the year.
- Are not required to file Form 4562, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-3 to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

A Principal business or profession, including product or service
SUSANNE PIERCE DIRECTOR

B Enter code from pages C-8 & 9
▶ 999999

C Business name. If no separate business name, leave blank.
SUSANNE PIERCE DIRECTOR

D Employer ID number (EIN), if any

E Business address (including suite or room no.). Address not required if same as on Form 1040, page 1.
310 BETHEL DRIVE

City, town or post office, state, and ZIP code
SALISBURY, NC 28144

Part II Figure Your Net Profit

1	Gross receipts. Caution: If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see Statutory Employee in the instructions for Schedule C, line 1, on page C-2 and check here ▶ ☐ SEE STATEMENT 16	1	9,000.
2	Total expenses. If more than $2,500, you must use Schedule C. See instructions.	2	0.
3	Net profit. Subtract line 2 from line 1. If less than zero, you must use Schedule C. Enter on Form 1040, line 12, and also on Schedule SE, line 2. (Statutory employees do not report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)	3	9,000.

Part III Information on Your Vehicle. Complete this part ONLY if you are claiming car or truck expenses on line 2.

4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ / /

5 Of the total number of miles you drove your vehicle during 1999, enter the number of miles you used your vehicle for:

a Business _____ b Commuting _____ c Other _____

6 Do you (or your spouse) have another vehicle available for personal use? ☐ Yes ☐ No

7 Was your vehicle available for use during off-duty hours? ☐ Yes ☐ No

8a Do you have evidence to support your deduction? ☐ Yes ☐ No

b If "Yes," is the evidence written? ☐ Yes ☐ No

3

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule C-EZ (Form 1040) 1999

9

11150404 767285 7020 1999.05300 PIERCE, ROBERT L 7020 1

DOJ-018215

SCHEDULE D (Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Capital Gains and Losses

▶ Attach to Form 1040. ▶ See Instructions for Schedule D (Form 1040).

1999

Attachment Sequence No. 12

ROBERT L. & SUSANNE D PIERCE

[redacted]

Part I Short-Term Capital Gains and Losses - Assets Held One Year or Less

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.) (c) Date sold	(d) Sales price	(e) Cost or other basis	(f) GAIN or (LOSS) Subtract (e) from (d)
1				
2 Enter your short-term totals	2			
3 Total short-term sales price amounts. Add column (d) of lines 1 and 2	3			
4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824			4	
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1		SEE STATEMENT 18	5	91,971.
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your 1998 Capital Loss Carryover Worksheet			6 ( )	
7 Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)		▶	7	91,971.

Part II Long-Term Capital Gains and Losses - Assets Held More Than One Year

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.) (c) Date sold	(d) Sales price	(e) Cost or other basis	(f) GAIN or (LOSS) Subtract (e) from (d)	(g) 28% RATE GAIN or (LOSS) * see instructions
8	03/03/97				
250 SHARES ATMEL CORP	08/12/99	9,003.	9,278.	<275.>	
100 SHARES HEWLETT PACKARD CO	10/09/96 07/19/99	11,512.	4,287.	7,225.	
85 SHARES PALOMAR MED TECH	01/15/96 12/10/99	93.	4,268.	<4,175.>	
200 SHARES PILLOWTEX CORP	11/21/97 12/10/99	994.	5,528.	<4,534.>	
9 Enter your long-term totals	9				
10 Total long-term sales price amounts. Add column (d) of lines 8 and 9	10	21,602.			
11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824		SEE STATEMENT 17	11	6,178.	
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1		SEE STATEMENT 19	12	<104,279.>	
13 Capital gain distributions		SEE STATEMENT 20	13	902.	
14 Long-term capital loss carryover. Enter in both columns (f) and (g) the amount, if any, from line 13 of your 1998 Capital Loss Carryover Worksheet			14 ( )	14,364.	14,364.
15 Combine lines 8 through 14 in column (g)			15		<14,364.>
16 Net long-term capital gain or (loss). Combine lines 8 through 14 in column (f) Next: Go to Part III on page 2		▶	16	<113,322.>	

* 28% Rate Gain or Loss includes all "collectibles gains and losses" and up to 50% of the eligible gain on qualified small business stock.

ROBERT L & SUSANNE D PIERCE [redacted]

Part III Summary of Parts I and II

17 Combine lines 7 and 16. If a loss, go to line 18. If a gain, enter the gain on Form 1040, line 13 — 17 <21,351.>

Next: Complete Form 1040 through line 35. Then, go to Part IV to figure your tax if

- Both lines 16 and 17 are gains, and
- Form 1040, line 35, is more than zero

18 If line 17 is a loss, enter here and as a (loss) on Form 1040, line 13, the smaller of these losses

- The loss on line 17, or
- ($3,000) or, if married filing separately, ($1,500) — 18 (3,000)

Next: Skip Part IV below. Instead, complete Form 1040 through line 37. Then, complete the Capital Loss Carryover Worksheet if

- The loss on line 17 exceeds the loss on line 18, or — SEE STATEMENT 21
- Form 1040, line 37, is a loss

Part IV Tax Computation Using Maximum Capital Gains Rates

19 Enter your taxable income from Form 1040, line 38 — 19
20 Enter the smaller of line 16 or line 17 of Schedule D — 20
21 If you are filing Form 4952, enter the amount from Form 4952, line 4e — 21
22 Subtract line 21 from line 20. If zero or less, enter -0- — 22
23 Combine line 7 and 13. If zero or less, enter -0- — 23
24 Enter the smaller of line 15 or line 23, but not less than zero — 24
25 Enter your unrecaptured section 1250 gain, if any, from line 16 of the worksheet — 25
26 Add lines 24 and 25 — 26
27 Subtract line 26 from line 22. If zero or less, enter -0- — 27
28 Subtract line 27 from line 19. If zero or less, enter -0- — 28
29 Enter the smaller of
- The amount on line 19, or
- $29,750 if single; $43,050 if married filing jointly or qualifying widow(er);
$21,525 if married filing separately; or $34,550 if head of household — 29
30 Enter the smaller of line 28 or line 29 — 30
31 Subtract line 27 from line 19. If zero or less, enter -0- — 31
32 Enter the larger of line 30 or line 31 — 32
33 Figure the tax on the amount on line 32. Use the Tax Table or Tax Rate Schedules, whichever applies — 33
Note. If line 29 is less than line 28, go to line 38
34 Enter the amount from line 29 — 34
35 Enter the amount from line 19 — 35
36 Subtract line 35 from line 34. If zero or less, enter -0- — 36
37 Multiply line 36 by 10% (.10) — 37
Note. If line 27 is more than zero and equal to line 36, go to line 52
38 Enter the smaller of line 19 or line 27 — 38
39 Enter the amount from line 36 — 39
40 Subtract line 39 from line 38 — 40
41 Multiply line 40 by 20% (.20) — 41
Note. If line 25 is zero or blank, skip lines 42 through 47 and read the note above line 48
42 Enter the smaller of line 22 or line 25 — 42
43 Add lines 22 and 32 — 43
44 Enter the amount from line 19 — 44
45 Subtract line 43 from line 44. If zero or less, enter -0- — 45
46 Subtract line 45 from line 42. If zero or less, enter -0- — 46
47 Multiply line 46 by 25% (.25) — 47
Note. If line 24 is zero or blank, go to line 52
48 Enter the amount from line 19 — 48
49 Add lines 32, 36, 40, and 46 — 49
50 Subtract line 49 from line 48 — 50
51 Multiply line 50 by 28% (.28) — 51
52 Add lines 33, 37, 41, 47, and 51 — 52
53 Figure the tax on the amount on line 19. Use the Tax Table or Tax Rate Schedules, whichever applies — 53
54 Tax on taxable income (including capital gains). Enter the smaller of line 52 or line 53 here and on Form 1040, line 40 — 54

SCHEDULE D (Form 1040)

ALTERNATIVE MINIMUM TAX
Capital Gains and Losses

1999

▶ Attach to Form 1040. ▶ See Instructions for Schedule D (Form 1040).

ROBERT L & SUZANNE D PIERCE

Part I Short-Term Capital Gains and Losses - Assets Held One Year or Less

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price	(e) Cost or other basis	(f) Gain or (loss) Subtract (e) from (d)	(g) 28% Rate Gain or (Loss) * (see instr. below)
1						
2 Enter your short-term totals		2				
3 Total short-term sales price amounts. Add column (d) of lines 1 and 2		3				
4 Short-term gain from Form 6252 and short-term gain or (loss) from Forms 4684, 6781, and 8824					4	
5 Net short-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1				SEE STATEMENT 25	5	91,971.
6 Short-term capital loss carryover. Enter the amount, if any, from line 8 of your 1998 Capital Loss Carryover Worksheet					6	
7 Net short-term capital gain or (loss). Combine lines 1 through 6 in column (f)				▶	7	91,971.

Part II Long-Term Capital Gains and Losses - Assets Held More Than One Year

(a) Description of property (Example: 100 sh. XYZ Co.)	(b) Date acquired (Mo., day, yr.)	(c) Date sold (Mo., day, yr.)	(d) Sales price	(e) Cost or other basis	(f) Gain or (loss) Subtract (e) from (d)	(g) 28% Rate Gain or (Loss) * (see instr. below)
6	03/03/97					
250 SHARES ATMEL CORP	08/12/99		9,001.	9,278.	<275.>	
100 SHARES HEWLETT PACKARD CO	10/09/96	07/19/99	11,512.	4,287.	7,225.	
85 SHARES PALOMAR MED TECH	01/15/99	12/10/99	93.	4,268.	<4,175.>	
200 SHARES PILLOWTEX CORP	11/21/97	12/10/99	994.	5,528.	<4,534.>	
9 Enter your long-term totals		9				
10 Total long-term sales price amounts. Add column (d) of lines 6 and 9		10	21,602.			
11 Gain from Form 4797, Part I; long-term gain from Forms 2439 and 6252; and long-term gain or (loss) from Forms 4684, 6781, and 8824				SEE STATEMENT 24	11	6,178.
12 Net long-term gain or (loss) from partnerships, S corporations, estates, and trusts from Schedule(s) K-1				SEE STATEMENT 22	12	<104,279.>
13 Capital gain distributions				SEE STATEMENT 23	13	902.
14 Long-term capital loss carryover. Enter in both columns (f) and (g) the amount, if any, from line 13 of your 1998 Capital Loss Carryover Worksheet					14	14,326. 14,326.
15 Combine lines 6 through 14 in column (g)					15	<14,326.>
16 Net long-term capital gain or (loss). Combine lines 6 through 14 in column (f)				▶	16	<113,284.>

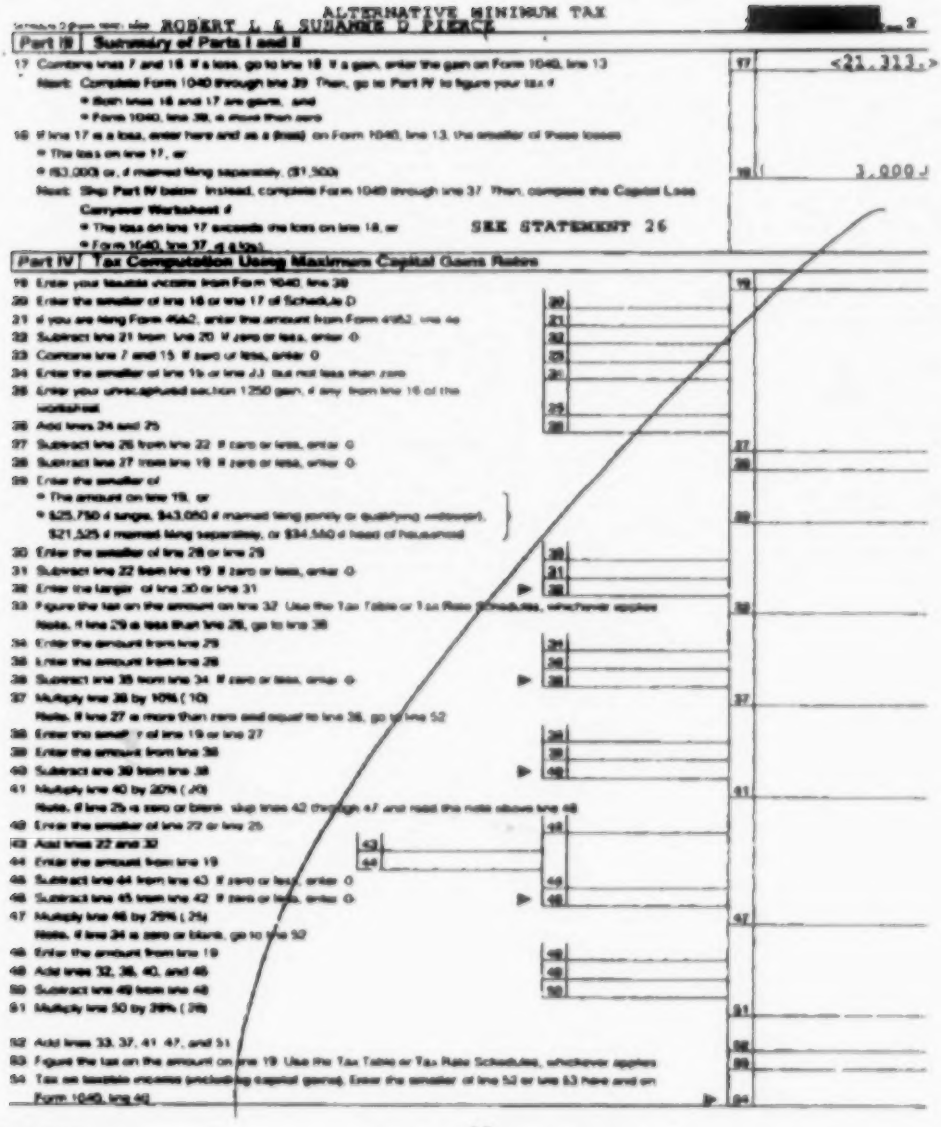
Next: Go to Part III on page 2

* 28% Rate Gain or Loss includes all "collectibles gains and losses" and up to 50% of the eligible gain on qualified small business stock

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule D (Form 1040) 1999

12
11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020___1

DOJ-018218



ALTERNATIVE MINIMUM TAX

ROBERT L & SUSANNE D PIERCE [redacted]

Part III Summary of Parts I and II

17 Combine lines 7 and 16. If a loss, go to line 18. If a gain, enter the gain on Form 1040, line 13 — 17 <21,313.>

Next: Complete Form 1040 through line 39. Then, go to Part IV to figure your tax if
- Both lines 16 and 17 are gains, and
- Form 1040, line 39, is more than zero

18 If line 17 is a loss, enter here and as a (loss) on Form 1040, line 13, the smaller of these losses — 18 (3,000)
- The loss on line 17, or
- ($3,000) or, if married filing separately, ($1,500)

Next: Skip Part IV below. Instead, complete Form 1040 through line 37. Then, complete the Capital Loss Carryover Worksheet if
- The loss on line 17 exceeds the loss on line 18, or SEE STATEMENT 26
- Form 1040, line 37, is a loss.

Part IV Tax Computation Using Maximum Capital Gains Rates

19 Enter your taxable income from Form 1040, line 39 — 19
20 Enter the smaller of line 16 or line 17 of Schedule D — 20
21 If you are filing Form 4952, enter the amount from Form 4952, line 4e — 21
22 Subtract line 21 from line 20. If zero or less, enter -0- — 22
23 Combine line 7 and 15. If zero or less, enter -0- — 23
24 Enter the smaller of line 15 or line 23, but not less than zero — 24
25 Enter your unrecaptured section 1250 gain, if any, from line 16 of the worksheet — 25
26 Add lines 24 and 25 — 26
27 Subtract line 26 from line 22. If zero or less, enter -0- — 27
28 Subtract line 27 from line 19. If zero or less, enter -0- — 28
29 Enter the smaller of
- The amount on line 19, or
- $425,750 if single, $43,050 if married filing jointly or qualifying widow(er), $21,525 if married filing separately, or $34,550 if head of household

29
30 Enter the smaller of line 28 or line 29 — 30
31 Subtract line 22 from line 19. If zero or less, enter -0- — 31
32 Enter the larger of line 30 or line 31 — 32
33 Figure the tax on the amount on line 32. Use the Tax Table or Tax Rate Schedules, whichever applies — 33
Note. If line 29 is less than line 28, go to line 38.
34 Enter the amount from line 29 — 34
35 Enter the amount from line 28 — 35
36 Subtract line 35 from line 34. If zero or less, enter -0- — 36
37 Multiply line 36 by 10% (.10) — 37
Note. If line 27 is more than zero and equal to line 36, go to line 52.
38 Enter the smaller of line 19 or line 27 — 38
39 Enter the amount from line 36 — 39
40 Subtract line 39 from line 38 — 40
41 Multiply line 40 by 20% (.20) — 41
Note. If line 25 is zero or blank, skip lines 42 through 47 and read the note above line 48.
42 Enter the smaller of line 22 or line 25 — 42
43 Add lines 22 and 32 — 43
44 Enter the amount from line 19 — 44
45 Subtract line 44 from line 43. If zero or less, enter -0- — 45
46 Subtract line 45 from line 42. If zero or less, enter -0- — 46
47 Multiply line 46 by 25% (.25) — 47
Note. If line 24 is zero or blank, go to line 52.
48 Enter the amount from line 19 — 48
49 Add lines 32, 36, 40, and 46 — 49
50 Subtract line 49 from line 48 — 50
51 Multiply line 50 by 28% (.28) — 51
52 Add lines 33, 37, 41, 47, and 51 — 52
53 Figure the tax on the amount on line 19. Use the Tax Table or Tax Rate Schedules, whichever applies — 53
54 Tax on taxable income (including capital gains). Enter the smaller of line 52 or line 53 here and on Form 1040, line 44 — 54

SCHEDULE E (Form 1040)

Supplemental Income and Loss

(From rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.)

1999

Attach to Form 1040 or Form 1041. See Instructions for Schedule E (Form 1040).

Attachment Sequence No. 13

Name(s) shown on return

ROBERT L & SUSANNE D PIERCE

Your social security number

[redacted]

Part I Income or Loss From Rental Real Estate and Royalties Note: Report income and expenses from your business of renting personal property on Schedule C or C-EZ. Report farm rental income or loss from Form 4835 on page 2, line 39.

	1 Show the kind and location of each rental real estate property:	2 For each rental real estate property listed on line 1, did you or your family use it during the tax year for personal purposes for more than the greater of • 14 days, or • 10% of the total days rented at fair rental value? (See page E-1.)	Yes	No
A	LAND LONG AND KERR STREETS SALISBURY, NC	A		X
B		B		
C		C		

Income:		Properties A	B	C	Totals (Add columns A, B, and C.)
3 Rents received	3	4,375.			3 4,375.
4 Royalties received	4				4
Expenses:					
5 Advertising	5				
6 Auto and travel (see page E-2)	6				
7 Cleaning and maintenance	7				
8 Commissions	8				
9 Insurance	9				
10 Legal and other professional fees	10				
11 Management fees	11				
12 Mortgage interest paid to banks, etc. (see page E-2)	12				12
13 Other interest	13				
14 Repairs	14				
15 Supplies	15				
16 Taxes	16				
17 Utilities	17				
18 Other (list) ▶	18				
19 Add lines 5 through 18	19				19
20 Depreciation expense or depletion (see page E-3)	20				20
21 Total expenses. Add lines 19 and 20	21				
22 Income or (loss) from rental real estate or royalty properties. Subtract line 21 from line 3 (rents) or line 4 (royalties). If the result is a (loss), see page E-3 to find out if you must file Form 6198	22	4,375.			
23 Deductible rental real estate loss. Caution: Your rental real estate loss on line 22 may be limited. See page E-3 to find out if you must file Form 8582. Real estate professionals must complete line 42 on page 2	23				
24 Income. Add positive amounts shown on line 22. Do not include any losses					24 4,375.
25 Losses. Add royalty losses from line 22 and rental real estate losses from line 23. Enter the total losses here					25 ( )
26 Total rental real estate and royalty income or (loss). Combine lines 24 and 25. Enter the result here. If Parts II, III, IV, and line 39 on page 2 do not apply to you, also enter this amount on Form 1040, line 17. Otherwise, include this amount in the total on line 40 on page 2					26 4,375.

For Paperwork Reduction Act Notice, see Form 1040 instructions. 14 Schedule E (Form 1040) 1999

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020 1

DOJ-018220

ROBERT L & SUSANNE D PIERCE

Part II Income or Loss From Partnerships and S Corporations

27	(a) Name	(b) Check if foreign partnership	(c) Employer identification number	Passive Income and Loss (d) Passive loss allowed	(e) Passive income from Schedule K-1	Nonpassive Income and Loss (f) Nonpassive loss from Schedule K-1	(g) Section 179 expense deduction from Form 4562	(h) Nonpassive income from Schedule K-1
A	SEE STATEMENT 27							
B								
C								
D								
E								
28a	Totals				5,119.	2,586.		368,087.
b	Totals			207.				
29	Add columns (g) and (i) of line 28a						29	371,206.
30	Add columns (f), (h), and (j) of line 28b						30	2,793.
31	Total partnership and S corporation income or (loss). Combine lines 29 and 30. Enter the result here and include in the total on line 40 below						31	370,413.

Part III Income or Loss From Estates and Trusts

32	(a) Name	(b) Employer identification number	Passive Income and Loss (c) Passive deduction or loss allowed	(d) Passive income from Schedule K-1	Nonpassive Income and Loss (e) Deduction or loss from Schedule K-1	(f) Other income from Schedule K-1
A						
B						
33a	Totals					
b	Totals					
34	Add columns (d) and (f) of line 33a					34
35	Add columns (c) and (e) of line 33b					35 ( )
36	Total estate and trust income or (loss). Combine lines 34 and 35. Enter the result here and include in the total on line 40 below					36

Part IV Income or Loss From Real Estate Mortgage Investment Conduits (REMICs) - Residual Holder

37	(a) Name	(b) Employer identification number	(c) Excess inclusion from Schedules Q, line 2c	(d) Taxable income (net loss) from Schedules Q, line 1b	(e) Income from Schedules Q, line 3b
38	Combine columns (d) and (e) only. Enter the result here and include in the total on line 40 below				38

Part V Summary

39	Net farm rental income or (loss) from Form 4835. Also, complete line 41 below		39
40	Total income or (loss). Combine lines 26, 31, 36, 38, and 39. Enter the result here and on Form 1040, line 17	▶	40 374,788.
41	Reconciliation of Farming and Fishing Income. Enter your gross farming and fishing income reported on Form 4835, line 7; Schedule K-1 (Form 1065), line 15b; Schedule K-1 (Form 1120S), line 23; and Schedule K-1 (Form 8141), line 14 (see page E-6)	41	
42	Reconciliation for Real Estate Professionals. If you were a real estate professional (see page E-6), enter the net income or (loss) you reported anywhere on Form 1040 from all rental real estate activities in which you materially participated under the passive activity loss rules	42	

Schedule E (Form 1040) 1999

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020 1

1999 Income from Passthroughs

DAVIDSON DIV R/E III,
I.D. NUMBER: 62-1262599
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

DAVIDSON DIV R/E III,

OTHER PASSIVE ACTIVITY

RENTAL REAL ESTATE INCOME (LOSS)	-170	
SCHEDULE E ACTIVITY INCOME (LOSS)		-170
ALLOWABLE PASSIVE LOSS FROM FORM 8582		-170

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	24

OTHER K-1 INFORMATION:

INTEREST - TOTAL	4
INVESTMENT INCOME	4

DOJ-018222

1999 Income from Passthroughs

HOME OIL & COAL
I.D. NUMBER: 56-0546791
TYPE: S CORPORATION

ACTIVITY INFORMATION:

HOME OIL & COAL

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	119,492	
SCHEDULE E ACTIVITY INCOME (LOSS)	119,492	

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	1,977
ADJUSTED GAIN OR LOSS	-167,386

OTHER K-1 INFORMATION:

INTEREST - TOTAL	-16,134
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	15,822
U.S. BONDS AND OBLIGATIONS	-29,956
SHORT-TERM CAPITAL GAIN (LOSS)	29,734
LONG-TERM CAPITAL GAIN (LOSS)	-42,425
CONTRIBUTIONS - 50% LIMITATION	571
SECTION 1231 GAIN (LOSS)	-29,867
MEDICAL PAYMENTS PAID ON BEHALF OF 2% SHAREHOLDER	1,462
NONDEDUCTIBLE EXPENSES	1,015

DOJ-018223

1999 Income from Passthroughs

PIERCE INVESTMENTS INC
I.D. NUMBER: 56-1724599
TYPE: S CORPORATION

ACTIVITY INFORMATION:

PIERCE INVESTMENTS INC		
RENTAL REAL ESTATE - ACTIVE PARTICIPATION		
RENTAL REAL ESTATE INCOME (LOSS)	5,119	
SCHEDULE K ACTIVITY INCOME (LOSS)	5,119	

OTHER K-1 INFORMATION:

INTEREST - TOTAL	788
LONG-TERM CAPITAL GAIN (LOSS)	27,000

DOJ-018224

1999 Income from Passthroughs

BO-BUCK MUTUAL INVESTMENT CLUB
I.D. NUMBER: 56-6098439
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

BO-BUCK MUTUAL INVESTMENT CLUB	
TRADE OR BUSINESS - MATERIAL PARTICIPATION	
OTHER PORTFOLIO/NONPORTFOLIO INCOME (LOSS)	1
SCHEDULE E ACTIVITY INCOME (LOSS)	1

OTHER K-1 INFORMATION:

DIVIDENDS - TOTAL	79
LONG-TERM CAPITAL GAIN (LOSS)	-52
DEDUCTIONS RELATED TO PORTFOLIO INCOME - 28	1

DOJ-018225

1999 Income from Passthroughs

[redacted] CONCRETE & SUPPLY LLC
I.D. NUMBER:
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

[redacted] CONCRETE & SUPPLY LLC

OTHER PASSIVE ACTIVITY

ORDINARY INCOME (LOSS)	-37	
SCHEDULE E ACTIVITY INCOME (LOSS)		-37
PASSIVE SECTION 1231 GAIN (LOSS)		-5
TOTAL ACTIVITY INCOME/LOSS		-42
ALLOWABLE PASSIVE LOSS FROM FORM 8582		-37

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	10
ADJUSTED GAIN OR LOSS	-31

OTHER K-1 INFORMATION:

INTEREST - TOTAL	-6
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	1
U.S. BONDS AND OBLIGATIONS	-5
SHORT-TERM CAPITAL GAIN (LOSS)	5
LONG-TERM CAPITAL GAIN (LOSS)	-8

DOJ-018226

1999 Income from Passthroughs

ROBERT L PIERCE GRANTOR TRUST B
I.D. NUMBER: 58-6388593
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

ROBERT L PIERCE GRANTOR TRUST B

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	-1,293	
SCHEDULE E ACTIVITY INCOME (LOSS)		-1,293

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	2,391
ADJUSTED GAIN OR LOSS	-175,080

OTHER K-1 INFORMATION:

INTEREST - TOTAL	31,655
DIVIDENDS - TOTAL	36,285
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	16,487
U.S. BONDS AND OBLIGATIONS	15,168
ORDINARY DIVIDENDS	1,605
TAX-EXEMPT INTEREST FROM 1099-DIV - STATE TAXABLE	34,680
SHORT-TERM CAPITAL GAIN (LOSS)	31,116
LONG-TERM CAPITAL GAIN (LOSS)	-44,397
CONTRIBUTIONS - 50% LIMITATION	594
NONPASSIVE ORDINARY ASSET GAIN (LOSS)	-38,418

DOJ-018227

1999 Income from Passthroughs

ROBERT L PIERCE GRANTOR TRUST B
I.D. NUMBER: 58-6388593
TYPE: S CORPORATION

ACTIVITY INFORMATION:

ROBERT L PIERCE GRANTOR TRUST B

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	124,297
SCHEDULE E ACTIVITY INCOME (LOSS)	124,297

DOJ-018228

1999 Income from Passthroughs

ROBERT L PIERCE GRANTOR TRUST A
I.D. NUMBER: 58-6388592
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

ROBERT L PIERCE GRANTOR TRUST A

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	-1,293	
SCHEDULE E ACTIVITY INCOME (LOSS)		-1,293

TAX PREFERENCE ITEMS:

BENEFICIARIES OF ESTATES AND TRUSTS	2,390
ADJUSTED GAIN OR LOSS	-175,078

OTHER K-1 INFORMATION:

INTEREST - TOTAL	31,653
DIVIDENDS - TOTAL	36,330
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	16,485
U.S. BONDS AND OBLIGATIONS	15,168
ORDINARY DIVIDENDS	1,650
TAX-EXEMPT INTEREST FROM 1099-DIV - STATE TAXABLE	34,680
SHORT-TERM CAPITAL GAIN (LOSS)	31,116
LONG-TERM CAPITAL GAIN (LOSS)	-44,397
CONTRIBUTIONS - 50% LIMITATION	594
NONPASSIVE ORDINARY ASSET GAIN (LOSS)	-36,417

DOJ-018229

1999 Income from Passthroughs

ROBERT L PIERCE GRANTOR TRUST A
I.D. NUMBER: 58-6388592
TYPE: S CORPORATION

ACTIVITY INFORMATION:

ROBERT L PIERCE GRANTOR TRUST A

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	124,297
SCHEDULE E ACTIVITY INCOME (LOSS)	124,297

DOJ-018230

1999 Income from Passthroughs

SUMMARY OF K-1 INFORMATION FOR ALL PASSTHROUGHS

OTHER K-1 INFORMATION:

INTEREST - TOTAL	69,962
DIVIDENDS - TOTAL	72,694
INTEREST AND DIVIDENDS DETAIL:	
SAVINGS/LOANS, BANK AND OTHER	69,587
U.S. BONDS AND OBLIGATIONS	375
ORDINARY DIVIDENDS	3,334
TAX-EXEMPT INTEREST FROM 1099-DIV - STATE TAXABLE	69,360
SHORT-TERM CAPITAL GAIN (LOSS)	91,971
LONG-TERM CAPITAL GAIN (LOSS)	-104,279
SECTION 1231 GAIN (LOSS)	-39,067
NONPASSIVE ORDINARY ASSET GAIN (LOSS)	-60,835
MEDICAL PAYMENTS PAID ON BEHALF OF 2% SHAREHOLDER	1,462
NONDEDUCTIBLE EXPENSES	1,015

DEDUCTIONS:

CONTRIBUTIONS - 50% LIMITATION	1,759
DEDUCTIONS RELATED TO PORTFOLIO INCOME - 2%	1

INVESTMENT INTEREST EXPENSE:

INVESTMENT INCOME	-14,114

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	4,402
BENEFICIARIES OF ESTATES AND TRUSTS	2,390
ADJUSTED GAIN OR LOSS	-517,495

DOJ-018231

SCHEDULE SE
(Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Self-Employment Tax

▶ See Instructions for Schedule SE (Form 1040).
▶ Attach to Form 1040.

OMB No. 1545-0074

1999

Name of person with self-employment income (as shown on Form 1040)

SUSANNE D PIERCE

Social security number of person with self-employment income ▶

[redacted]

Who Must File Schedule SE

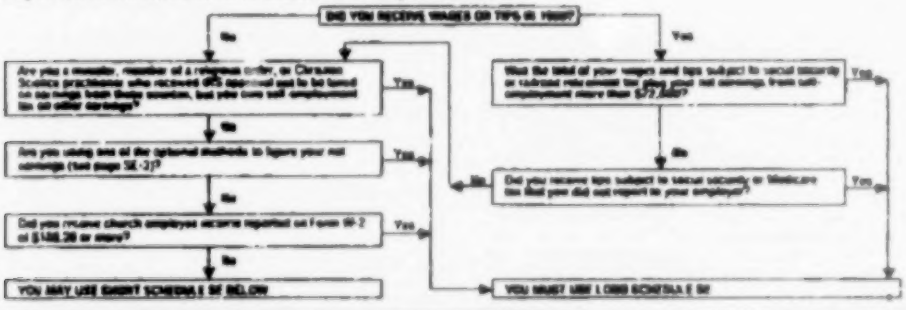
You must file Schedule SE if:

- You had net earnings from self-employment from other than church employee income (line 4 of Short Schedule SE or line 4c of Long Schedule SE) of $400 or more, OR
- You had church employee income of $108.28 or more. Income from services you performed as a minister or a member of a religious order is not church employee income. See page SE-1.

Note: Even if you had a loss or a small amount of income from self-employment, it may be to your benefit to file Schedule SE and use either "optional method" in Part II of Long Schedule SE. See page SE-3.

Exception. If your only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner and you filed Form 4361 and received IRS approval not to be taxed on those earnings, do not file Schedule SE. Instead, write "Exempt Form 4361" on Form 1040, line 50.

May I Use Short Schedule SE or MUST I Use Long Schedule SE?



Section A - Short Schedule SE. Caution: *Read above to see if you can use Short Schedule SE*

1	Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a	1	
2	Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report. START 28	2	9,000.
3	Combine lines 1 and 2	3	9,000.
4	Net earnings from self-employment. Multiply line 3 by 92.35% (.9235). If less than $400, do not file this schedule; you do not owe self-employment tax. ▶	4	8,312.
5	Self-employment tax. If the amount on line 4 is: • $72,600 or less, multiply line 4 by 15.3% (.153). Enter the result here and on Form 1040, line 55. • More than $72,600, multiply line 4 by 2.9% (.029). Then, add $9,002.40 to the result. Enter the total here and on Form 1040, line 55.	5	1,272.
6	Deduction for one-half of self-employment tax. Multiply line 5 by 50% (.5). Enter the result here and on Form 1040, line 27	6	636.

LHA For Paperwork Reduction Act Notice, see Form 1040 instructions. Schedule SE (Form 1040) 1999

Schedule SE (Form 1040) 1999 Attachment Sequence No. 17 18 Page 2

Name of person with self-employment income (as shown on Form 1040)	Social security number of person with self-employment income ▶
ROBERT L PIERCE	[redacted]

Section B - Long Schedule SE

Part I Self-Employment Tax

Note: *If your only income subject to self-employment tax is church employee income, skip lines 1 through 4b. Enter -0- on line 4c and go to line 5a. Income from services you performed as a minister or a member of a religious order is not church employee income. See page SE-1.*

A	If you are a minister, member of a religious order, or Christian Science practitioner and you filed Form 4361 but you had $400 or more of other net earnings from self-employment, check here and continue with Part I ▶ ☐		
1	Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a. Note: *Skip this line if you use the farm optional method. See page SE-3.*	1	
2	Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report. Note: *Skip this line if you use the nonfarm optional method. See page SE-3.* SEE STATEMENT 29	2	9,600.
3	Combine lines 1 and 2	3	9,600.
4a	If line 3 is more than zero, multiply line 3 by 92.35% (.9235). Otherwise, enter amount from line 3	4a	8,866.
b	If you elected one or both of the optional methods, enter the total of lines 15 and 17 here	4b	
c	Combine lines 4a and 4b. If less than $400, do not file this schedule; you do not owe self-employment tax. Exception: If less than $400 and you had church employee income, enter -0- and continue ▶	4c	8,866.
5a	Enter your church employee income from Form W-2. Caution: See page SE-1 for definition of church employee income. 5a		
b	Multiply line 5a by 92.35% (.9235). If less than $100, enter -0-	5b	
6	Net earnings from self-employment. Add lines 4c and 5b	6	8,866.
7	Maximum amount of combined wages and self-employment earnings subject to social security tax or the 6.2% portion of the 7.65% railroad retirement (tier 1) tax for 1999	7	72,600.00
8a	Total social security wages and tips (total of boxes 3 and 7 on Form(s) W-2) and railroad retirement (tier 1) compensation. 8a 72,600.		
b	Unreported tips subject to social security tax (from Form 4137, line 9). 8b		
c	Add lines 8a and 8b	8c	72,600.
9	Subtract line 8c from line 7. If zero or less, enter -0- here and on line 10 and go to line 11 ▶	9	0.
10	Multiply the smaller of line 6 or line 9 by 12.4% (.124)	10	0.
11	Multiply line 6 by 2.9% (.029)	11	257.
12	Self-employment tax. Add lines 10 and 11. Enter here and on Form 1040, line 50	12	257.
13	Deduction for one-half of self-employment tax. Multiply line 12 by 50% (.5). Enter the result here and on Form 1040, line 27 13 129.		

Part II Optional Methods To Figure Net Earnings (see page SE-3.)

Farm Optional Method. *You may use this method only if*
- *Your gross farm income[1] was not more than $2,400, or*
- *Your net farm profits[2] were less than $1,733.*

14	Maximum income for optional methods	14 1,600.00
15	Enter the smaller of: two-thirds (2/3) of gross farm income[1] (not less than zero) or $1,600. Also include this amount on line 4b above	15

Nonfarm Optional Method. *You may use this method only if*
- *Your net nonfarm profits[3] were less than $1,733 and also less than 72.189% of your gross nonfarm income,[4] and*
- *You had net earnings from self-employment of at least $400 in 2 of the prior 3 years.*

Caution: You may use this method no more than five times.

16	Subtract line 15 from line 14	16
17	Enter the smaller of: two-thirds (2/3) of gross nonfarm income[3] (not less than zero) or the amount on line 16. Also include this amount on line 4b above	17

[1] From Sch. F, line 11, and Sch. K-1 (Form 1065), line 15a.
[2] From Sch. F, line 36, and Sch. K-1 (Form 1065), line 15a.
[3] From Sch. C, line 31; Sch. C-EZ, line 3; Sch. K-1 (Form 1065), line 15a; and Sch. K-1 (Form 1065-B), box 9.
[4] From Sch. C, line 7; Sch. C-EZ, line 1; Sch. K-1 (Form 1065), line 15c; and Sch. K-1 (Form 1065-B), box 9.

Schedule SE (Form 1040) 1999

27

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020___1

DOJ-018233

Form **1116** — **Foreign Tax Credit** — **1999**

(Individual, Estate, Trust, or Nonresident Alien Individual)

▶ Attach to Form 1040, 1040NR, 1041, or 990-T.

Name

ROBERT L & SUSANNE D PIERCE

Identifying number as shown on page 1 of your return

[redacted]

Use a separate Form 1116 for each category of income listed below. See Categories of Income on page 3 of the instructions. Check only one box on each Form 1116. Report all amounts in U.S. dollars except where specified in Part II below.

a ☐ Passive income
b ☐ High withholding tax interest
c ☐ Financial services income
d ☐ Shipping income
e ☐ Dividends from a DISC or former DISC
f ☐ Certain distributions from a foreign sales corporation (FSC) or former FSC
g ☐ Lump sum distributions
h ☐ Section 901(j) income
i ☐ Income re-sourced by treaty
j ☒ General limitation income

1 Resident of (name of country) ▶ **US**

Note: If you paid taxes to only one foreign country or U.S. possession, use column A in Part I and line A in Part II. If you paid taxes to more than one foreign country or U.S. possession, use a separate column and line for each country or possession.

Part I Taxable Income or Loss From Sources Outside the United States (for Category Checked Above)

	Foreign Country or U.S. Possession A	B	C	Total (Add cols. A, B, and C)
1 Enter the name of the foreign country or U.S. possession ▶	MEXICO			
1 Gross income from sources within country shown above and of the type checked above:	328.			1 328.
Deductions and losses:				
2 Expenses definitely related to the income on line 1 (attach statement)				
3 Pro rata share of other deductions not definitely related:				
a Certain itemized deductions or standard deduction	122,515.			
b Other deductions (attach statement)				
c Add lines 3a and 3b	122,515.			
d Gross foreign source income	328.			
e Gross income from all sources	901,715.			
f Divide line 3d by line 3e	.000364			
g Multiply line 3c by line 3f	45.			
4 Pro rata share of interest expense:				
a Home mortgage interest (see worksheet on page 9 of the instructions)				
b Other interest expense				
5 Losses from foreign sources				
6 Add lines 2, 3g, 4a, 4b, and 5	45.			6 45.
7 Subtract line 6 from line 1. Enter the result here and on line 10, page 2				▶ 7 283.

Part II Foreign Taxes Paid or Accrued

Credit is claimed for taxes (you must check one)	Foreign taxes paid or accrued — In foreign currency: Taxes withheld at source on: (c) Dividends; (d) Rents and royalties; (e) Interest; (f) Other foreign taxes paid or accrued	In U.S. dollars: Taxes withheld at source on: (g) Dividends 25.; (h) Rents and royalties; (i) Interest; (j) Other foreign taxes paid or accrued	(k) Total foreign taxes paid or accrued (add cols. (g) through (j))
(a) ☒ Paid (b) ☐ Accrued			
A			25.
B			
C			
D			
E			
F			
G			
H			
8 Add lines A through G, column (k). Enter the total here and on line 9, page 2		▶ 8	25.

LHA For Paperwork Reduction Act Notice, see separate instructions. Form 1116 (1999)

Form 1116 (1999) ROBERT L & SUSANNE D PIERCE Page 3

Part III Figuring the Credit

9	Enter amount from line 8. These are your total foreign taxes paid or accrued for the category of income checked above Part I	9	25.	
10	Carryback or carryover (attach detailed computation)	10		
11	Add lines 9 and 10	11	25.	
12	Reduction in foreign taxes	12		
13	Subtract line 12 from line 11. This is the total amount of foreign taxes available for credit			13 25.
14	Enter amount from line 7. This is your taxable income or (loss) from sources outside the United States (before adjustments) for the category of income checked above Part I.	14	283.	
15	Adjustments to line 14	15		
16	Combine the amounts on lines 14 and 15. This is your net foreign source taxable income. (If the result is zero or less, you have no foreign tax credit for the category of income you checked above Part I. Skip lines 17 through 21.)	16	283.	
17	Individuals. Enter amount from Form 1040, line 37. If you are a non-resident alien, enter amount from Form 1040NR, line 36. Estates and trusts. Enter your taxable income without the deduction for your exemption. Caution: If you figured your tax using the special rates on capital gains, see instructions	17	502,826.	
18	Divide line 16 by line 17. If line 16 is more than line 17, enter "1"			18 .000563
19	Individuals: Enter amount from Form 1040, line 48, less any amounts on Form 1040, lines 41 through 45, and any mortgage interest credit (from Form 8396) and District of Columbia first-time homebuyer credit (from Form 8859) on line 47. If you are a nonresident alien, enter amount from Form 1040NR, line 38, less any amount on Form 1040NR, lines 40, 41, 42, and any mortgage interest credit (from Form 8396) and District of Columbia first-time homebuyer credit (from Form 8859) on line 44. Estates and trusts: Enter amount from Form 1041, Schedule G, line 1c, or Form 990-T, lines 35 and 37			19 172,280.
20	Multiply line 19 by line 18 (maximum amount of credit)			20 97.
21	Enter the amount from line 13 or line 20, whichever is smaller. If this is the only Form 1116 you are completing, skip lines 22 through 23 and enter this amount on line 24. Otherwise, complete the applicable line of Part IV	▶		21 25.

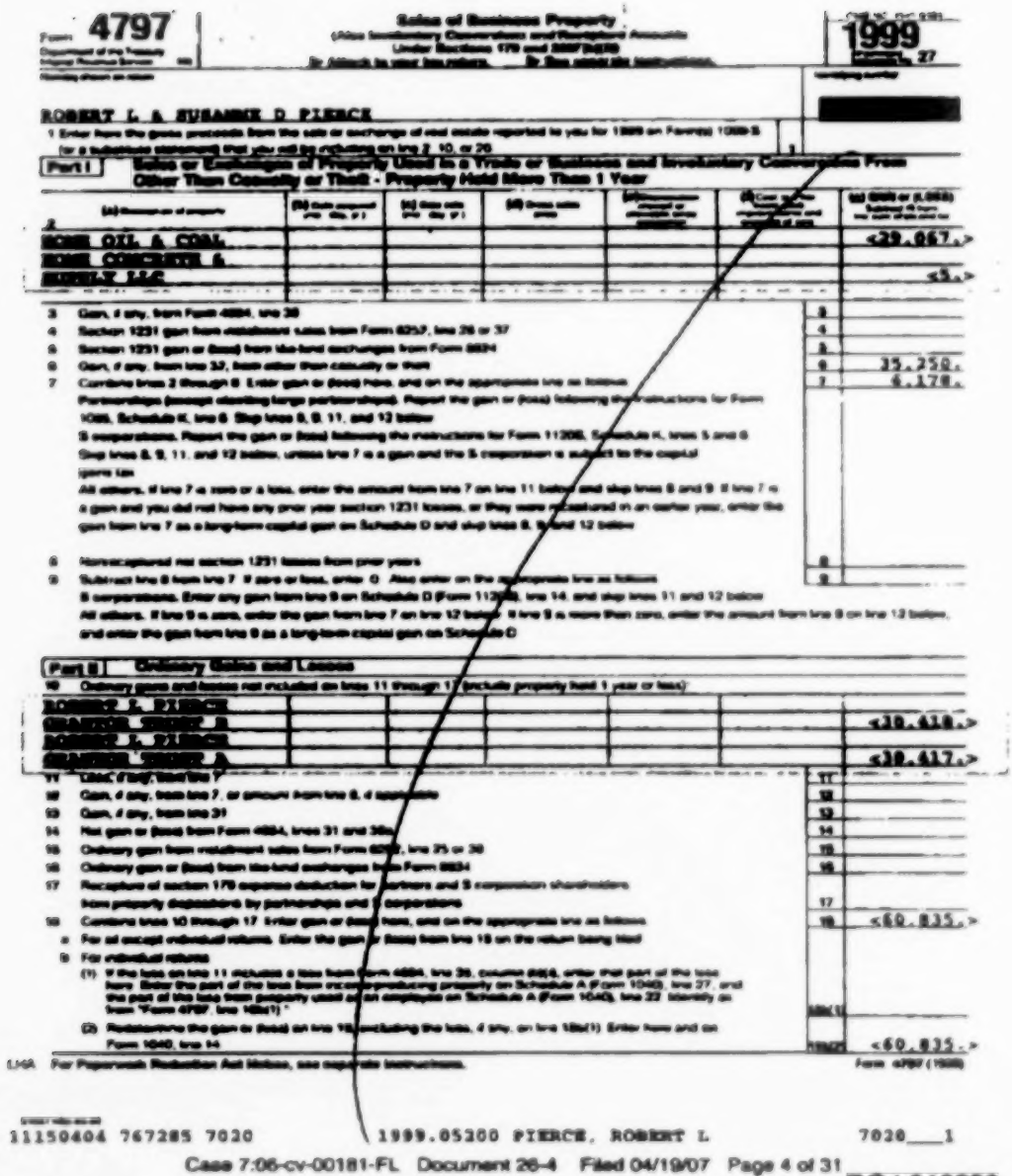
Part IV Summary of Credits From Separate Parts III

22	Credit for taxes on passive income	22	0.
23	Credit for taxes on high withholding tax interest	23	0.
24	Credit for taxes on financial services income	24	0.
25	Credit for taxes on shipping income	25	0.
26	Credit for taxes on dividends from a DISC or former DISC and certain distributions from a FSC or former FSC	26	0.
27	Credit for taxes on lump sum distributions	27	0.
28	Credit for taxes on income re-sourced by treaty	28	0.
29	Credit for taxes on general limitation income	29	25.
30	Add lines 22 through 29		30 25.
31	Reduction of credit for international boycott operations		31
32	Subtract line 31 from line 30. This is your foreign tax credit. Enter here and on Form 1040, line 46; Form 1040NR, line 43; Form 1041, Schedule G, line 2a; or Form 990-T, line 36	▶	32 25.

Form 1116 (1999)

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020___1

DOJ-018235



Form 4797 — Sales of Business Property — 1999

ROBERT L & SUSANNE D PIERCE

Part I — Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft - Property Held More Than 1 Year

(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) Gain or (loss) Subtract (f) from the sum of (d) and (e)
2						
HOME OIL & COAL						<29,067.>
HOME CONCRETE &						
SUPPLY LLC						<5.>

3	Gain, if any, from Form 4684, line 39	3	
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4	
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5	
6	Gain, if any, from line 32, from other than casualty or theft	6	35,250.
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows: Partnerships (except electing large partnerships). Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 6. Skip lines 8, 9, 11, and 12 below. S corporations. Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax. All others. If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	7	6,178.
8	Nonrecaptured net section 1231 losses from prior years	8	
9	Subtract line 8 from line 7. If zero or less, enter 0. Also enter on the appropriate line as follows: S corporations. Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below. All others. If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D	9	

Part II — Ordinary Gains and Losses

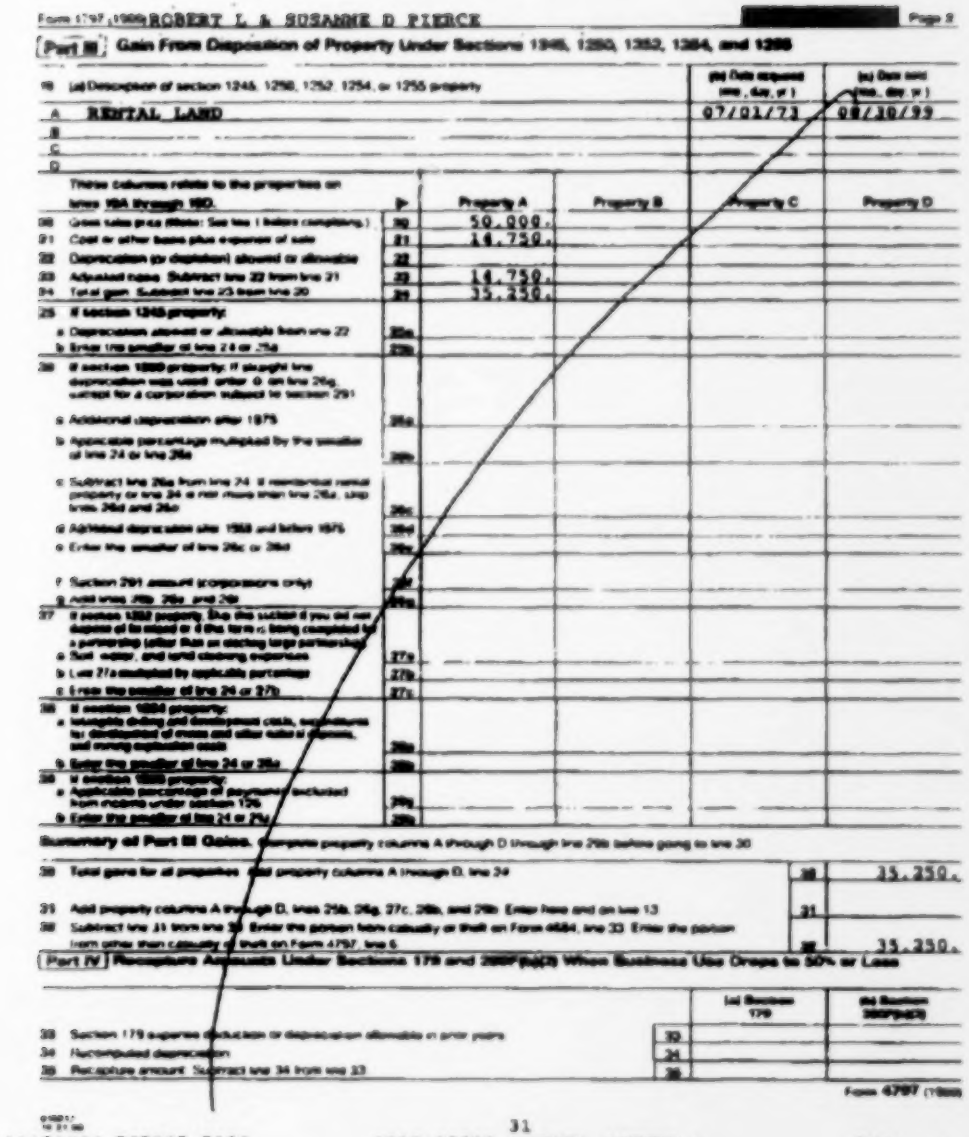
10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

ROBERT L PIERCE							
GRANTOR TRUST A							<10,418.>
ROBERT L PIERCE							
GRANTOR TRUST A							<10,417.>

11	Loss, if any, from line 7	11	
12	Gain, if any, from line 7, or amount from line 8, if applicable	12	
13	Gain, if any, from line 31	13	
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16	
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations	17	
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18	<60,835.>
a	For all except individual returns. Enter the gain or (loss) from line 18 on the return being filed		
b	For individual returns: (1) If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18(b)(1)."	18b(1)	
	(2) Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)	<60,835.>

LHA For Paperwork Reduction Act Notice, see separate instructions. Form 4797 (1999)

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020___1



Form 4797 (1999) ROBERT L & SUSANNE D PIERCE [redacted] Page 2

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A RENTAL LAND	07/01/73	08/30/99
B		
C		
D		

These columns relate to the properties on lines 19A through 19D.		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20	50,000.			
21 Cost or other basis plus expense of sale	21	14,750.			
22 Depreciation (or depletion) allowed or allowable	22				
23 Adjusted basis. Subtract line 22 from line 21	23	14,750.			
24 Total gain. Subtract line 23 from line 20	24	35,250.			
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a				
b Enter the smaller of line 24 or 25a	25b				
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	35,250.
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	35,250.

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation	34		
35 Recapture amount. Subtract line 34 from line 33	35		

Form 4797 (1999)

Form **6198** — **At-Risk Limitations** — ▶ Attach to your tax return. — OMB No. 1545-0144 — **1999** — Attachment Sequence No. **31**

ROBERT L PIERCE — Identifying number: [redacted]

DAVIDSON DIV B/E III

Part I Current Year Profit (Loss) From the Activity, Including Prior Year Nondeductible Amounts. (Enter losses in parentheses.)

1	Ordinary income (loss) from the activity	1	<170.>
2	Gain (loss) from the sale or other disposition of assets used in the activity (or of your interest in the activity) that you actually will be reporting on.		
a	Schedule D	2a	
b	Form 4797	2b	
c	Other form or schedule	2c	
3	Other income or gains from the activity, from Schedule K-1 of Form 1065, Form 1065-B, or Form 1120S, that were not included above on lines 1 through 2c	3	4.
4	Other deductions or losses from the activity, excluding investment interest expense allowed from Form 4952, that were not used in ignoring amounts on lines 1 through 3	4	( )
5	Current year profit (loss) from the activity. Combine lines 1 through 4. See instructions before completing the rest of the form.	5	<166.>

Part II Simplified Computation of Amount At Risk

6	Adjusted basis (as defined in section 1011) in the activity (or in your interest in the activity) on the first day of the tax year. Do not enter less than zero	6	1,737.
7	Increases for the tax year	7	
8	Add lines 6 and 7	8	1,737.
9	Decreases for the tax year — SEE STATEMENT 30	9	3.
10a	Subtract line 9 from line 8 ▶ 10a 1,734.		
b	If line 10a is greater than zero, enter that amount here and go to line 20 (or complete Part III). Otherwise, enter -0- and see Pub. 925 for information on the recapture rules. *Note: You may want to use Part III to see if it gives you a larger amount at risk.*	10b	1,734.

Part III Detailed Computation of Amount At Risk

(If you completed Part III of Form 6198 for 1998, see instructions for Part III for 1999.)

11	Investments in the activity (or in your interest in the activity) at the effective date. Do not enter less than zero	11	
12	Increases at effective date	12	
13	Add lines 11 and 12	13	
14	Decreases at effective date	14	
15	Amount at risk (check box that applies): a ☐ At effective date: Subtract line 14 from line 13. Do not enter less than zero. b ☐ From 1998 Form 6198, line 19b, enter the amount from line 19b of the 1998 form.)	15	
16	Increases since (check box that applies): a ☐ Effective date b ☐ The end of your 1998 tax year	16	
17	Add lines 15 and 16	17	
18	Decreases since (check box that applies): a ☐ Effective date b ☐ The end of your 1998 tax year	18	
19a	Subtract line 18 from line 17 ▶ 19a		
b	If line 19a is greater than zero, enter that amount here and go to line 20. Otherwise, enter -0- and see Pub. 925 for information on the recapture rules.	19b	

Part IV Deductible Loss

20	Amount at risk. Enter the larger of line 10b or line 19b	20	1,734.
21	Deductible losses. If line 20 is zero, enter -0-. You do not have a deductible loss this year. Otherwise, enter the smaller of the line 5 loss (treated as a positive number) or line 20. See the instructions for how to report any deductible loss and any carryover. **LOSS(ES) FULLY DEDUCTIBLE**	21	(166.)

Note: If this loss is from a passive activity, see Form 8582, Passive Activity Loss Limitations, or Form 8810, Corporate Passive Activity Loss and Credit Limitations, to find out if the loss is allowed under the passive activity rules. If only part of the loss is subject to the passive activity loss rules, report only that part on Form 8582 or Form 8810, whichever applies.

LHA For Paperwork Reduction Act Notice, see page 7 — Form 6198 (1999)

ALTERNATIVE MINIMUM TAX

Form **6198**

At-Risk Limitations

▶ Attach to your tax return.

OMB No. 1545-0712

1999

Attachment Sequence No. **31**

Name(s) shown on return

Identifying number

ROBERT L PIERCE

DAVIDSON DIV R/E III.

Part I Current Year Profit (Loss) From the Activity, Including Prior Year Nondeductible Amounts. (Enter losses in parentheses.)

1	Ordinary income (loss) from the activity	1	<146.>
2	Gain (loss) from the sale or other disposition of assets used in the activity (or of your interest in the activity) that you usually will be reporting on:		
a	Schedule D	2a	
b	Form 4797	2b	
c	Other form or schedule	2c	
3	Other income or gains from the activity, both Schedule K-1 of Form 1065, Form 1065-B, or Form 1120S, that were not included above on lines 1 through 2c	3	4.
4	Other deductions or losses from the activity, including investment interest expense allowed from Form 4952, that were not used in reporting amounts on lines 1 through 3	4	( )
5	Current year profit (loss) from the activity. Combine lines 1 through 4. See instructions before completing the rest of this form	5	<142.>

Part II Simplified Computation of Amount At Risk

6	Adjusted basis (as defined in section 1011) in the activity (or in your interest in the activity) on the last day of the tax year. Do not enter less than zero	6	3,822.
7	Increases for the tax year	7	
8	Add lines 6 and 7	8	3,822.
9	Decreases for the tax year	9	3.
10a	Subtract line 9 from line 8 ▶ 10a | 3,819.		
b	If line 10a is greater than zero, enter that amount here and go to line 26 (or complete Part III). Otherwise, enter -0- and see Pub. 925 for information on the exception rules. Note: You may want to use Part III to see if it gives you a larger amount at risk	10b	3,819.

Part III Detailed Computation of Amount At Risk

(If you completed Part III of Form 6198 for 1998, see instructions for Part III for 1999.)

11	Investment in the activity (or in your interest in the activity) at the effective date. Do not enter less than zero	11	
12	Increases at effective date	12	
13	Add lines 11 and 12	13	
14	Decreases at effective date	14	
15	Amount at risk (check box that applies): a ☐ At effective date. Subtract line 14 from line 13. Do not enter less than zero. b ☐ From 1998 Form 6198, line 15b. (Do not enter the amount from line 14b of the 1998 form.)	15	
16	Increases since (check box that applies): a ☐ (Effective date) b ☐ The end of your 1998 tax year	16	
17	Add lines 15 and 16	17	
18	Decreases since (check box that applies): a ☐ (Effective date) b ☐ The end of your 1998 tax year	18	
19a	Subtract line 18 from line 17 ▶ 19a |		
b	If line 19a is more than zero, enter that amount here and go to line 20. Otherwise, enter -0- and see Pub. 925 for explanation on the exception rules	19b	

Part IV Deductible Loss

20	Amount at risk. Enter the larger of line 10b or line 19b	20	3,819.
21	Deductible loss. If line 20 is zero, enter -0-. You do not have a deductible loss this year. Otherwise, enter the smaller of the line 5 loss (treated as a positive number) or line 20. See the instructions for how to report any deductible loss and pay carryover **LOSS(ES) FULLY DEDUCTIBLE**	21	(142.)

Note: If this loss is from a passive activity, see Form 8582, Passive Activity Loss Limitations, or Form 8810, Corporate Passive Activity Loss and Credit Limitations, to find out if the loss is allowed under the passive activity rules. If only part of the loss is subject to the passive activity loss rules, report only that part on Form 8582 or Form 8810, whichever applies.

LHA For Paperwork Reduction Act Notice, see page 7. Form 6198 (1999)

Form 1116 — ALTERNATIVE MINIMUM TAX — Foreign Tax Credit — 1999

ROBERT L & SUSANNE D PIERCE

[redacted]

a ☐ Passive income
b ☐ High withholding tax interest
c ☐ Financial services income
d ☐ Shipping income
e ☐ Dividends from a DISC or former DISC
f ☐ Certain distributions from a foreign sales corporation (FSC) or former FSC
g ☐ Lump-sum distributions
h ☐ Section 901(j) income
i ☐ Income re-sourced by treaty
j ☒ General limitation income

1 Name of country ▶ US

Note: If you paid taxes to only one foreign country or U.S. possession, use column A in Part I and line 8 in Part II. If you paid taxes to more than one foreign country or U.S. possession, use a separate column and line for each country or possession.

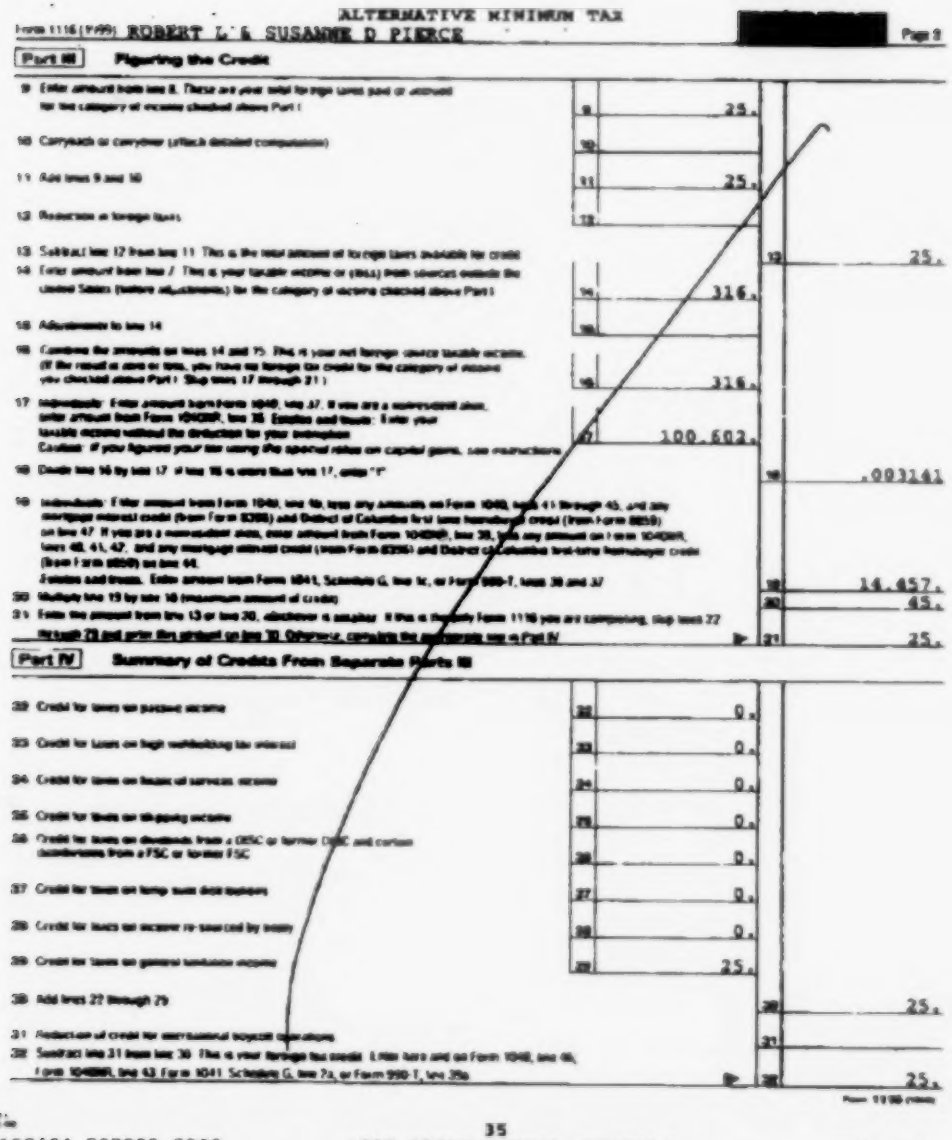
Part I Taxable Income or Loss From Sources Outside the United States (for Category Checked Above)

	Foreign Country or U.S. Possession A	B	C	Total (Add cols. A, B, and C.)
1 Enter the name of the foreign country or U.S. possession ▶	MEXICO			
1 Gross income from sources within country shown above and of the type checked above:	328.			1 328.
Deductions and losses:				
2 Expenses definitely related to the income on line 1 (attach statement)	0.			
3 Pro rata share of other deductions not definitely related:				
a Certain itemized deductions or standard deduction	14,144.			
b Other deductions (attach statement)	0.			
c Add lines 3a and 3b	14,144.			
d Gross foreign source income	328.			
e Gross income from all sources	384,289.			
f Divide line 3d by line 3e	.000854			
g Multiply line 3c by line 3f	12.			
4 Pro rata share of interest expense:				
a Home mortgage interest (see worksheet on page 9 of the instructions)				
b Other interest expense	0.			
5 Losses from foreign sources	0.			
6 Add lines 2, 3g, 4a, 4b, and 5	12.			6 12.
7 Subtract line 6 from line 1. Enter the result here and on line 14, page 2				▶ 7 316.

Part II Foreign Taxes Paid or Accrued

Country (Enter two-letter code for the foreign country or U.S. possession in which taxes were paid or accrued)	(a) Check if taxes were (Paid / Accrued)	Foreign taxes paid or accrued — In foreign currency: Taxes withheld at source on (b) Dividends	(c) Rents and royalties	(d) Interest	(e) Other foreign taxes paid or accrued	In U.S. dollars: Taxes withheld at source on (f) Dividends	(g) Rents and royalties	(h) Interest	(i) Other foreign taxes paid or accrued	(j) Total foreign taxes paid or accrued (add cols. (f) through (i))
A MX	☒ Paid ☐ Accrued					25.				25.
B	☐ Paid ☐ Accrued									
C	☐ Paid ☐ Accrued									
8 Add lines A through C, columns (a). Enter the total here and on line 3, page 2									▶ 8	25.

LHA For Paperwork Reduction Act Notice, see separate instructions. Form 1116 (1999)



ALTERNATIVE MINIMUM TAX

Form 1116 (1999) ROBERT L & SUSANNE D PIERCE [redacted] Page 2

Part III Figuring the Credit

9 Enter amount from line 8. These are your total foreign taxes paid or accrued for the category of income checked above Part I	9	25.	
10 Carryback or carryover (attach detailed computation)	10		
11 Add lines 9 and 10	11	25.	
12 Reduction in foreign taxes	12		
13 Subtract line 12 from line 11. This is the total amount of foreign taxes available for credit			13 25.
14 Enter amount from line 7. This is your taxable income or (loss) from sources outside the United States (before adjustments) for the category of income checked above Part I	14	316.	
15 Adjustments to line 14	15		
16 Combine the amounts on lines 14 and 15. This is your net foreign source taxable income. If the result is zero or less, you have no foreign tax credit for the category of income you checked above Part I. Skip lines 17 through 21	16	316.	
17 Individuals: Enter amount from Form 1040, line 37. If you are a nonresident alien, enter amount from Form 1040NR, line 36. Estates and trusts: Enter your taxable income without the deduction for your exemption. Caution: If you figured your tax using the special rates on capital gains, see instructions	17	100,602.	
18 Divide line 16 by line 17. If line 16 is more than line 17, enter "1"			18 .003141
19 Individuals: Enter amount from Form 1040, line 40, less any amounts on Form 1040, lines 41 through 45, and any mortgage interest credit (from Form 8396) and District of Columbia first-time homebuyer credit (from Form 8859) on line 47. If you are a nonresident alien, enter amount from Form 1040NR, line 38, less any amount on Form 1040NR, lines 40, 41, 42, and any mortgage interest credit (from Form 8396) and District of Columbia first-time homebuyer credit (from Form 8859) on line 44. Estates and trusts: Enter amount from Form 1041, Schedule G, line 1a; or Form 990-T, lines 36 and 37			19 14,457.
20 Multiply line 19 by line 18 (maximum amount of credit)			20 45.
21 Enter the amount from line 13 or line 20, whichever is smaller. If this is the only Form 1116 you are completing, skip lines 22 through 29 and enter this amount on line 30. Otherwise, complete the worksheet next on Part IV	▶		21 25.

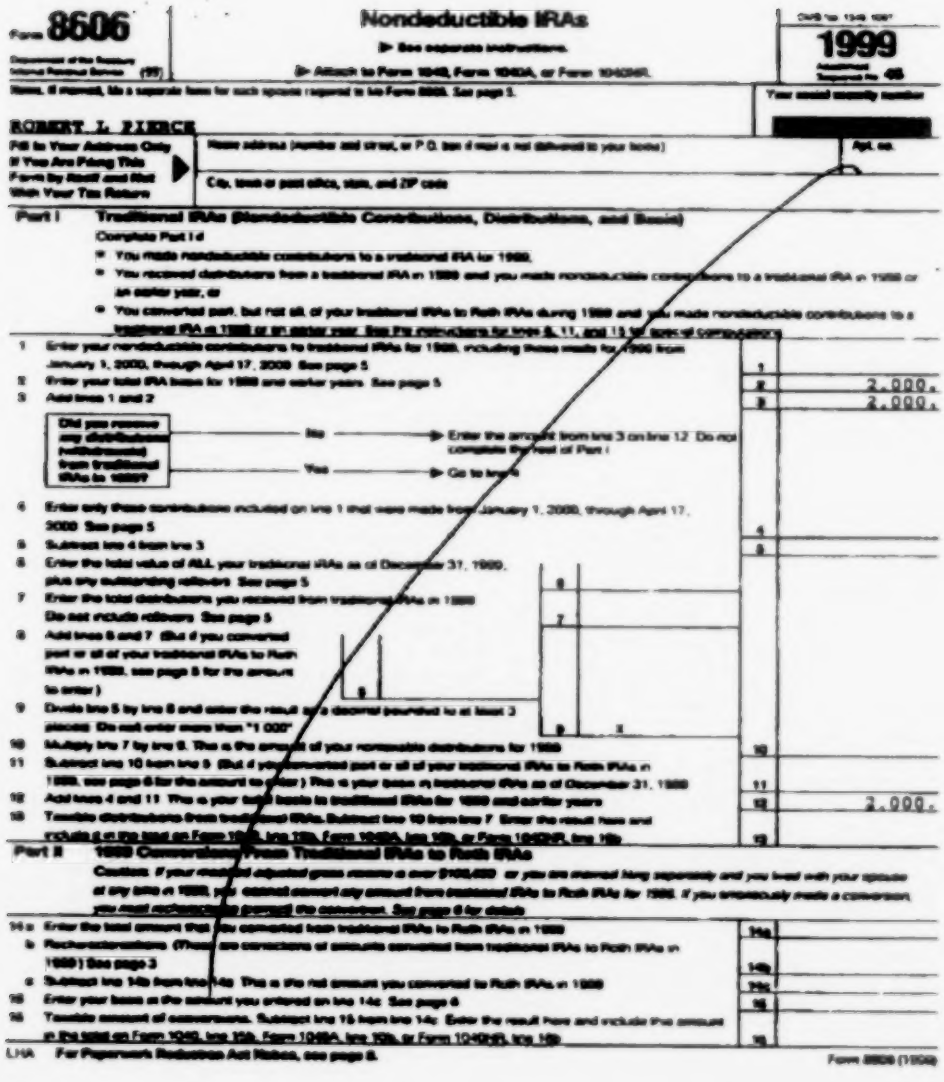
Part IV Summary of Credits From Separate Parts III

22 Credit for taxes on passive income	22	0.	
23 Credit for taxes on high withholding tax interest	23	0.	
24 Credit for taxes on financial services income	24	0.	
25 Credit for taxes on shipping income	25	0.	
26 Credit for taxes on dividends from a DISC or former DISC and certain distributions from a FSC or former FSC	26	0.	
27 Credit for taxes on lump sum distributions	27	0.	
28 Credit for taxes not assigned to separate categories	28	0.	
29 Credit for taxes on general limitation income	29	25.	
30 Add lines 22 through 29			30 25.
31 Reduction of credit for international boycott operations			31
32 Subtract line 31 from line 30. This is your foreign tax credit. Enter here and on Form 1040, line 46; Form 1040NR, line 43; Form 1041 Schedule G, line 2a; or Form 990-T, line 36a	▶		32 25.

Form 1116 (1999)

11150406 767285 7020 1999.05200 PIERCE, ROBERT L 7020 1

DOJ-018241



Form 8606 Nondeductible IRAs

▶ See separate instructions.

▶ Attach to Form 1040, Form 1040A, or Form 1040NR.

1999

ROBERT L PIERCE

Fill In Your Address Only If You Are Filing This Form by Itself and Not With Your Tax Return

Home address (number and street, or P.O. box if mail is not delivered to your home) Apt. no.

City, town or post office, state, and ZIP code

Part I Traditional IRAs (Nondeductible Contributions, Distributions, and Basis)

Complete Part I if

- You made nondeductible contributions to a traditional IRA for 1999.
- You received distributions from a traditional IRA in 1999 and you made nondeductible contributions to a traditional IRA in 1999 or an earlier year, or
- You converted part, but not all, of your traditional IRAs to Roth IRAs during 1999 and you made nondeductible contributions to a traditional IRA in 1999 or an earlier year. See the instructions for lines 6, 11, and 13 for special computations.

1	Enter your nondeductible contributions to traditional IRAs for 1999, including those made by April 17, 2000	1	
2	Enter your total IRA basis for 1999 and earlier years. See page 5	2	2,000.
3	Add lines 1 and 2	3	2,000.
	Did you receive any distributions (withdrawals) from traditional IRAs in 1999? No ▶ Enter the amount from line 3 on line 12. Do not complete the rest of Part I. Yes ▶ Go to line 4.		
4	Enter only those contributions included on line 1 that were made from January 1, 2000, through April 17, 2000. See page 5	4	
5	Subtract line 4 from line 3	5	
6	Enter the total value of ALL your traditional IRAs as of December 31, 1999, plus any outstanding rollovers. See page 5	6	
7	Enter the total distributions you received from traditional IRAs in 1999. Do not include rollovers. See page 5	7	
8	Add lines 6 and 7. (But if you converted part or all of your traditional IRAs to Roth IRAs in 1999, see page 6 for the amount to enter.)	8	
9	Divide line 5 by line 8 and enter the result as a decimal rounded to at least 3 places. Do not enter more than "1.000"	9	.
10	Multiply line 7 by line 9. This is the amount of your nontaxable distributions for 1999	10	
11	Subtract line 10 from line 5. (But if you converted part or all of your traditional IRAs to Roth IRAs in 1999, see page 6 for the amount to enter.) This is your basis in traditional IRAs as of December 31, 1999	11	
12	Add lines 4 and 11. This is your total basis in traditional IRAs for 1999 and earlier years	12	2,000.
13	Taxable distributions from traditional IRAs. Subtract line 10 from line 7. Enter the result here and include it on line 15a of Form 1040, line 15b of Form 1040A, line 15b of Form 1040EZ, or line 16b of Form 1040NR.	13	

Part II 1999 Conversions From Traditional IRAs to Roth IRAs

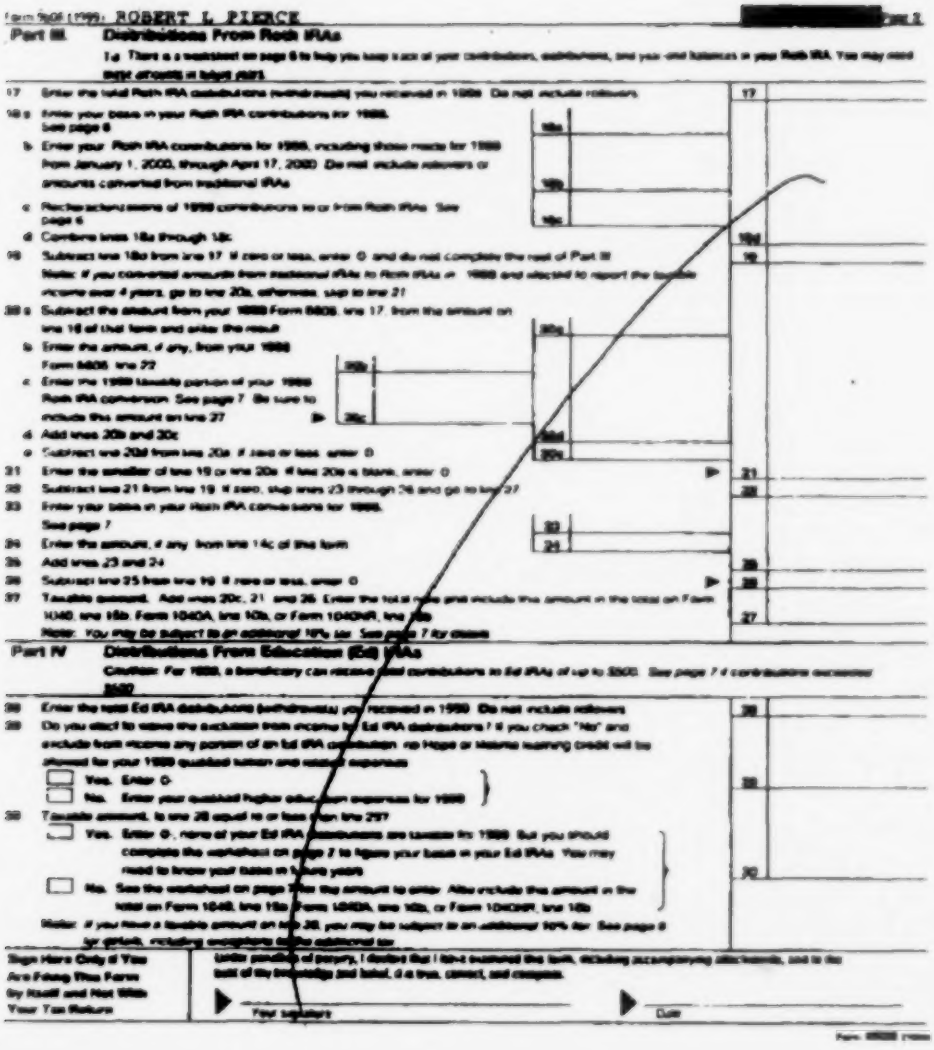
Caution: If your modified adjusted gross income is over $100,000 or you are married filing separately and you lived with your spouse at any time in 1999, you cannot convert any amount from traditional IRAs to Roth IRAs for 1999. If you unintentionally made a conversion, you must recharacterize it (correct the conversion). See page 6 for details.

14a	Enter the total amount that you converted from traditional IRAs to Roth IRAs in 1999	14a	
b	Recharacterizations. (These are corrections of amounts converted from traditional IRAs to Roth IRAs in 1999.) See page 3	14b	
c	Subtract line 14b from line 14a. This is the net amount you converted to Roth IRAs in 1999	14c	
15	Enter your basis in the amount you entered on line 14c. See page 6	15	
16	Taxable amount of conversions. Subtract line 15 from line 14c. Enter the result here and include this amount in the total on Form 1040, line 15b, Form 1040A, line 15b, or Form 1040NR, line 16b	16	

LHA For Paperwork Reduction Act Notice, see page 8. Form 8606 (1999)

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020___1

DOJ-018242



Form 8606 (1999) ROBERT L PIERCE [redacted] Page 2

Part III Distributions From Roth IRAs

1a There is a worksheet on page 6 to help you keep track of your contributions, distributions, and your year-end balances in your Roth IRA. You may need many amounts in future years.

17 Enter the total Roth IRA distributions (withdrawals) you received in 1999. Do not include rollovers. 17

18 a Enter your basis in your Roth IRA contributions for 1998. See page 6 18a

b Enter your Roth IRA contributions for 1999, including those made for 1998 from January 1, 2000, through April 17, 2000. Do not include rollovers or amounts converted from traditional IRAs 18b

c Reache actions exams of 1999 contributions to or from Roth IRAs. See page 6 18c

d Combine lines 18a through 18c 18d

19 Subtract line 18d from line 17. If zero or less, enter 0 and do not complete the rest of Part III 19

Note: If you converted amounts from traditional IRAs to Roth IRAs in 1998 and elected to report the taxable income over 4 years, go to line 20a; otherwise, skip to line 21.

20 a Subtract the amount from your 1998 Form 8606, line 17, from the amount on line 18 of that form and enter the result 20a

b Enter the amount, if any, from your 1998 Form 8606, line 22 20b

c Enter the 1999 taxable portion of your 1998 Roth IRA conversion. See page 7. Be sure to include this amount on line 27 20c

d Add lines 20b and 20c 20d

e Subtract line 20d from line 20a. If zero or less, enter 0 20e

21 Enter the smaller of line 19 or line 20e. If line 20e is blank, enter 0 21

22 Subtract line 21 from line 19. If zero, skip lines 23 through 26 and go to line 27 22

23 Enter your basis in your Roth IRA conversions for 1998. See page 7 23

24 Enter the amount, if any, from line 14c of this form 24

25 Add lines 23 and 24 25

26 Subtract line 25 from line 19. If zero or less, enter 0 26

27 Taxable amount. Add lines 20c, 21, and 26. Enter the total here and include this amount in the total on Form 1040, line 15b; Form 1040A, line 10b; or Form 1040NR, line 16b. 27

Note: You may be subject to an additional 10% tax. See page 7 for details.

Part IV Distributions From Education (Ed) IRAs

Caution: For 1998, a beneficiary can receive Ed IRA contributions of up to $500. See page 7 if contributions exceeded $500.

28 Enter the total Ed IRA distributions (withdrawals) you received in 1999. Do not include rollovers. 28

29 Do you elect to waive the exclusion from income for Ed IRA distributions? If you check "No" and include in income any portion of an Ed IRA contribution, no Hope or Lifetime learning credit will be allowed for your 1999 qualified tuition and related expenses.

☐ Yes. Enter 0. 29

☐ No. Enter your qualified higher education expenses for 1999

30 Taxable amount, is line 28 equal to or less than line 29?

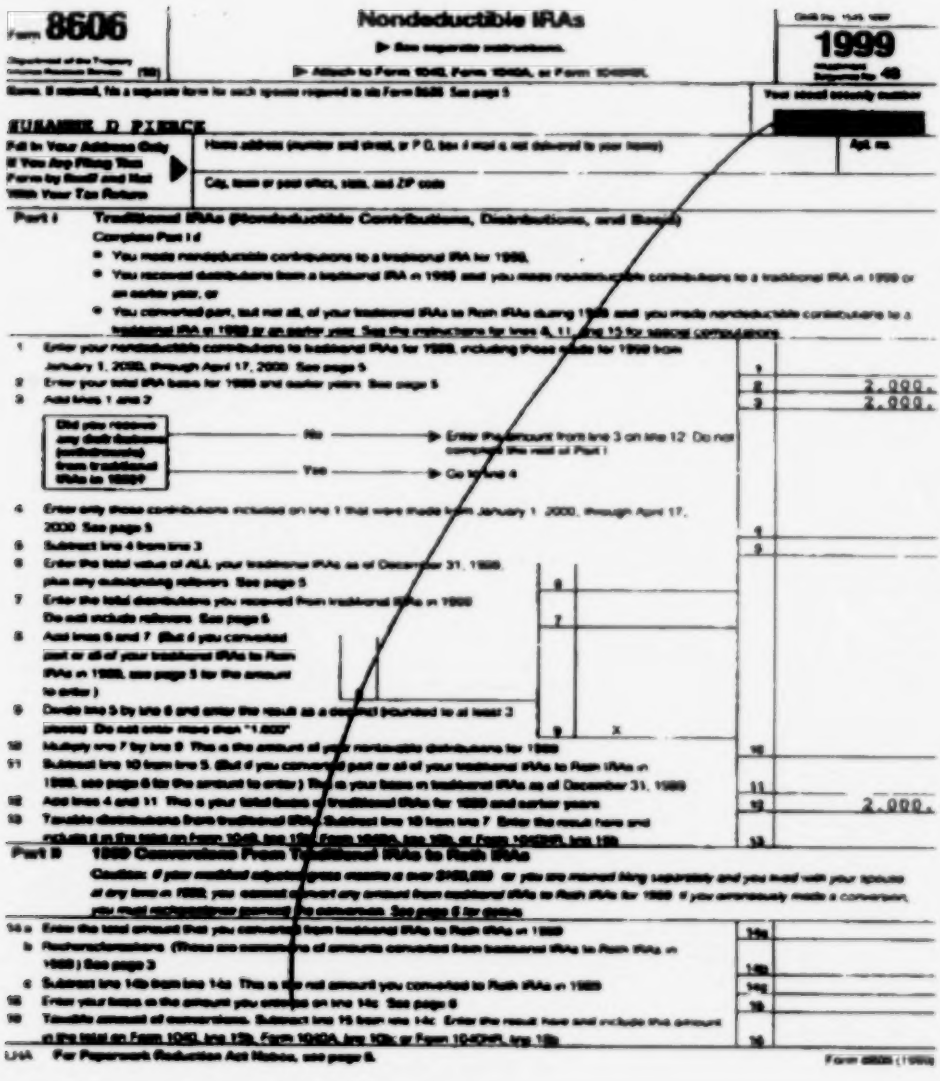
☐ Yes. Enter 0. None of your Ed IRA distributions are taxable for 1999. But you should complete the worksheet on page 7 to figure your basis in your Ed IRAs. You may need to know your basis in future years.

☐ No. See the worksheet on page 7 for the amount to enter. Also include this amount in the total on Form 1040, line 15b; Form 1040A, line 10b; or Form 1040NR, line 16b. 30

Note: If you have a taxable amount on line 30, you may be subject to an additional 10% tax. See page 8 for details, including exceptions to the additional tax.

Sign Here Only if You Are Filing This Form by Itself and Not With Your Tax Return	Under penalties of perjury, I declare that I have examined this form, including accompanying attachments, and to the best of my knowledge and belief, it is true, correct, and complete. Your signature ▶ Date ▶

Form 8606 (1999)



Form 8606 Nondeductible IRAs

▶ See separate instructions.

▶ Attach to Form 1040, Form 1040A, or Form 1040NR.

1999

Attachment Sequence No. 48

Name. If married, file a separate form for each spouse required to file Form 8606. See page 5

Your social security number

SUSANNE D PIERCE

Fill in Your Address Only If You Are Filing This Form by Itself and Not With Your Tax Return

Home address (number and street, or P.O. box if mail is not delivered to your home)

Apt. no.

City, town or post office, state, and ZIP code

Part I Traditional IRAs (Nondeductible Contributions, Distributions, and Basis)

Complete Part I if

- You made nondeductible contributions to a traditional IRA for 1999,
- You received distributions from a traditional IRA in 1999 and you made nondeductible contributions to a traditional IRA in 1999 or an earlier year, or
- You converted part, but not all, of your traditional IRAs to Roth IRAs during 1999 and you made nondeductible contributions to a traditional IRA in 1999 or an earlier year. See the instructions for lines 4, 11, and 15 for special computations.

1 Enter your nondeductible contributions to traditional IRAs for 1999, including those made for 1999 from January 1, 2000, through April 17, 2000. See page 5 — 1

2 Enter your total IRA basis for 1999 and earlier years. See page 5 — 2 — 2,000.

3 Add lines 1 and 2 — 3 — 2,000.

Did you receive any distributions (withdrawals) from traditional IRAs in 1999?

No ▶ Enter the amount from line 3 on line 12. Do not complete the rest of Part I

Yes ▶ Go to line 4

4 Enter only those contributions included on line 1 that were made from January 1, 2000, through April 17, 2000. See page 5 — 4

5 Subtract line 4 from line 3 — 5

6 Enter the total value of ALL your traditional IRAs as of December 31, 1999, plus any outstanding rollovers. See page 5 — 6

7 Enter the total distributions you received from traditional IRAs in 1999. Do not include rollovers. See page 6 — 7

8 Add lines 6 and 7. (But if you converted part or all of your traditional IRAs to Roth IRAs in 1999, see page 6 for the amount to enter.) — 8

9 Divide line 5 by line 8 and enter the result as a decimal (rounded to at least 3 places). Do not enter more than "1.000" — 9 X

10 Multiply line 7 by line 9. This is the amount of your nontaxable distributions for 1999 — 10

11 Subtract line 10 from line 5. (But if you converted part or all of your traditional IRAs to Roth IRAs in 1999, see page 6 for the amount to enter.) This is your basis in traditional IRAs as of December 31, 1999 — 11

12 Add lines 4 and 11. This is your total basis in traditional IRAs for 1999 and earlier years — 12 — 2,000.

13 Taxable distributions from traditional IRAs. Subtract line 10 from line 7. Enter the result here and include it on the total on Form 1040, line 15b; Form 1040A, line 10b; or Form 1040NR, line 16b — 13

Part II 1999 Conversions From Traditional IRAs to Roth IRAs

Caution: If your modified adjusted gross income is over $100,000 or you are married filing separately and you lived with your spouse at any time in 1999, you cannot convert any amount from traditional IRAs to Roth IRAs for 1999. If you erroneously made a conversion, you must recharacterize your payment. See page 6 for details.

14a Enter the total amount that you converted from traditional IRAs to Roth IRAs in 1999 — 14a

b Recharacterizations. (These are corrections of amounts converted from traditional IRAs to Roth IRAs in 1999.) See page 3 — 14b

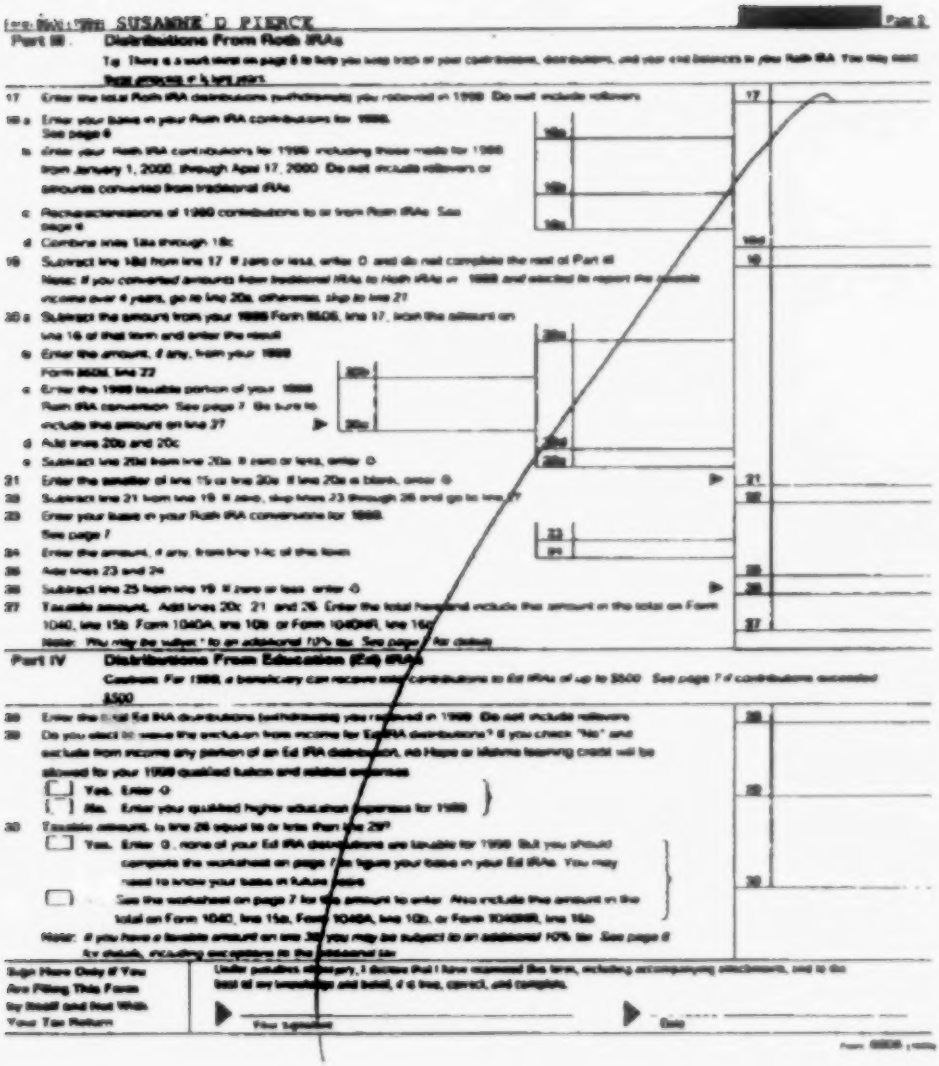
c Subtract line 14b from line 14a. This is the net amount you converted to Roth IRAs in 1999 — 14c

15 Enter your basis in the amount you entered on line 14c. See page 6 — 15

16 Taxable amount of conversions. Subtract line 15 from line 14c. Enter the result here and include this amount in the total on Form 1040, line 15b; Form 1040A, line 10b; or Form 1040NR, line 16b — 16

For Paperwork Reduction Act Notice, see page 8.

Form 8606 (1999)



SUSANNE D PIERCE

Part III Distributions From Roth IRAs

Part IV Distributions From Education (Ed) IRAs

Sign Here Only If You Are Filing This Form by Itself and Not With Your Tax Return

Form 8283 (Rev. October 1998)
Department of the Treasury
Internal Revenue Service

Noncash Charitable Contributions

▶ Attach to your tax return if you claimed a total deduction of over $500 for all contributed property.

OMB No. 1545-0908

Attachment Sequence No. 55

Identifying number

Name(s) shown on your income tax return

ROBERT L & SUSANNE D PIERCE

Note: Figure the amount of your contribution deduction before completing this form. See your tax return instructions.

Section A - List in this section only items (or groups of similar items) for which you claimed a deduction of $5,000 or less. Also, list certain publicly traded securities even if the deduction is over $5,000 (see instructions).

Part I Information on Donated Property - If you need more space, attach a statement.

	(a) Name and address of the donee organization	(b) Description of donated property
A	SALISBURY COMMUNITY FOUNDATION CHARLOTTE NC	500 SHARES DELHAIZE AMERICA CLASS B STOCK
B	GOODWILL SALISBURY, NC	CLOTHES
C		
D		
E		

Note: If you answered "Yes" to line 2 for property listed in Part I, you do not have to complete columns (c), (d), (e), and (f).

	(c) Date of the contribution	(d) Date acquired (mo., yr.)	(e) How acquired by donor	(f) Donor's cost or adjusted basis	(g) Fair market value	(h) Method used to determine the fair market value
A	12/27/99	06/85	PURCHASE	1,000.	10,454.	COMPARABLE SALES
B			PURCHASE	2,000.	500.	THRIFT SHOP VALUE
C						
D						
E						

Part II Other Information - Complete line 2 if you gave less than an entire interest in property listed in Part I.
Complete line 3 if conditions were attached to a contribution listed in Part I.

2 If, during the year, you contributed less than the entire interest in the property, complete lines a - c.
a Enter the letter from Part I that identifies the property ▶ _____. If Part II applies to more than one property, attach a separate statement.
b Total amount claimed as a deduction for the property listed in Part I: (1) For this tax year ▶ _____
(2) For any prior tax years ▶ _____
c Name and address of each organization to which any such contribution was made in a prior year (complete only if different than the donee organization above)

Name of charitable organization (donee)

Address (number, street, and room or suite no.)

City or town, state, and ZIP code

3 For tangible property, enter the place where the property is located or kept ▶ _____
4 Name of any person, other than the donee organization, having actual possession of the property ▶ _____

		Yes	No
5	If conditions were attached to any contribution listed in Part I, answer questions a - c and attach the required statement (see instructions).		
a	Is there a restriction, either temporary or permanent, on the donee's right to use or dispose of the donated property?		
b	Did you give to anyone (other than the donee organization or another organization participating with the donee organization in cooperative fundraising) the right to the income from the donated property or to the possession of the property, including the right to vote donated securities, to acquire the property by purchase or otherwise, or to designate the person having such income, possession, or right to acquire?		
c	Is there a restriction limiting the donated property for a particular use?		

LHA For Paperwork Reduction Act Notice, see separate instructions. Form 8283 (Rev. 10-98)

11150404 767285 7020 40 1999.05200 PIERCE, ROBERT L 7020___1

DOJ-018246

Form **8271** (Rev. July 1998)
Department of the Treasury
Internal Revenue Service

Investor Reporting of Tax Shelter Registration Number

▶ Attach to your tax return

OMB No. 1545-1051

Attachment Sequence No. 77

ROBERT L & SUSANNE D PIERCE

[redacted] 12/31/99

	(a) Tax Shelter Name	(b) Tax Shelter Registration Number (11-digit number)	(c) Tax Shelter Identifying Number
1	DAVIDSON DIV R/E III.	852480000094	62-1262599
2			
3			
4			
5			
6			
7			
8			
9			
10			

Form 1116 U.S. and Foreign Source Income Summary

[redacted]

ROBERT L & SUZANNE D PIERCE

INCOME TYPE	TOTAL	US	FOREIGN GENERAL
Compensation	147,449.	147,449.	
Dividends/Distributions	82,477.	82,477.	
Interest	69,027.	69,027.	
Capital Gains	135,348.	135,348.	
Pensions/Annuities	18,600.	18,600.	
Rent/Royalty	4,375.	4,375.	
Taxable Local Refunds			
Partnership/S Corporation	373,206.	373,206.	
Trust/Estate			
Other Income	30.	<298.>	328.
Nontaxable Income	71,203.	71,203.	
Gross Income	901,715.	901,387.	328.
Less:			
Section 911 Exclusion			
Capital Losses	138,348.	138,348.	
Capital Gain Tax Adjustment			
Nontaxable Income	71,203.	71,203.	
Total Income - Form 1116	692,164.	691,836.	328.
Deductions:			
Business/Profession Expenses			
Rent/Royalty Expenses			
Partnership/S Corporation Losses	2,793.	2,793.	
Trust/Estate Losses			
Capital Losses			
Non-capital Losses	60,835.	60,835.	
Individual Retirement Account			
Moving Expenses			
Self-employment Tax Deduction	765.	765.	
Self-employment Health Insurance			
Keogh Contributions	2,326.	2,326.	
Alimony			
Forfeited Interest			
Foreign Housing Deduction			
Other Adjustments			
Capital Gains Tax Adjustment			
Total Deductions	66,719.	66,719.	
Adjusted Gross Income	625,445.	625,117.	328.
Less Itemized Deductions			
Specifically Allocated			
Home Mortgage Interest	104.	104.	
Other Interest			
Pro-rata Allocated	122,515.	122,470.	45.
Total Adjustments to Adjusted Gross Income	122,619.	122,574.	45.
Taxable Income Before Exemptions	502,826.	502,541.	283.

Form 1116 — Allocation of Itemized Deductions

ROBERT L & SUSANNE D PIERCE [redacted]

	Form Itemized Deductions	Itemized Deductions After Sec 68 Reduction	Form 1116		
			Specifically U.S.	Specifically Foreign	Residual
Taxes	123,323.	109,909.			109,909.
Interest - Not Including Investment Interest	117.	104.	104.		
Contributions	14,144.	12,606.			12,606.
Miscellaneous Deductions Subject to 2%					
Other Miscellaneous Deductions - Not Including Gambling Losses					
Foreign Adjustment					
Total Itemized Deductions Subject to Sec 68	137,584.	122,619.			
Add Itemized Deductions Not Subject to Sec 68					
Medical/Dental					
Investment Interest					
Casualty Losses					
Gambling Losses					
Foreign Adjustment					
Total Itemized Deductions	137,584.				
Total Allowed on Schedule A		122,619.	104.		122,515.

Form 1116 — Foreign Tax Preference Items

ROBERT L & SUSANNE D PIERCE [redacted]

Itemized deductions		14,144.
Other deductions not directly allocated		0.
Total alternative minimum tax adjustments		14,144.
Total foreign source income	329.	
Total gross income	184,289.	
Ratio of foreign source income to gross income		.000858
Total foreign source deductions		12.

Total deductions allocable to foreign income class

Gross investment income	12.
Passive income	
Dividends from a DISC or former DISC	
Distributions of a FSC	
High withholding tax interest	
Financial services income	
Shipping income	
Section 901(j) income	
Income re-sourced by treaty	

11150404 767285 7020 1999.05200 PIERCE, ROBERT L 7020 1

DOJ-018250

ROBERT L & SUSANNE D PIERCE [redacted]

FOOTNOTES STATEMENT 1

DURING THE YEAR THE PROCEEDS OF A SHORT SALE NOT CLOSED BY THE TAXPAYER IN THIS TAX YEAR WERE RECEIVED.

ROBERT L & SUSANNE D PIERCE [redacted]

FORM 1040	PENSIONS AND ANNUITIES	STATEMENT 2
PRUDENTIAL INS CO		
AMOUNT RECEIVED THIS YEAR	30.	
NONTAXABLE AMOUNT		
CAPITAL GAIN DISTRIBUTION REPORTED ON SCH D		
AMOUNT INCLUDED IN FORM 1040, LINE 16B		30.
HOME OIL & COAL 401K PROFIT SHARING PLAN		
AMOUNT RECEIVED THIS YEAR	4,691.	
NONTAXABLE AMOUNT (ROLLOVER)	4,691.	
CAPITAL GAIN DISTRIBUTION REPORTED ON SCH D		
AMOUNT INCLUDED IN FORM 1040, LINE 16B		0.
TOTAL INCLUDED IN FORM 1040, LINE 16B		30.

ROBERT L & SUSANNE D PIERCE [redacted]

FORM 1040 PERSONAL EXEMPTION WORKSHEET STATEMENT 3

1.	IS THE AMOUNT ON FORM 1040, LINE 34, MORE THAN THE AMOUNT SHOWN ON LINE 4 BELOW FOR YOUR FILING STATUS? NO. STOP. MULTIPLY $2,750 BY THE TOTAL NUMBER OF EXEMPTIONS CLAIMED ON FORM 1040, LINE 6D, AND ENTER THE RESULT ON LINE 38. YES. GO TO LINE 2.			
2.	MULTIPLY $2,750 BY THE TOTAL NUMBER OF EXEMPTIONS CLAIMED ON FORM 1040, LINE 6D			5,500.
3.	ENTER THE AMOUNT FROM FORM 1040, LINE 34 . .		625,445.	
4.	ENTER THE AMOUNT FOR YOUR FILING STATUS . .		189,950.	a
	MARRIED FILING SEPARATE	$ 94,975		
	SINGLE	$126,600		
	HEAD OF HOUSEHOLD	$158,300		
	MARRIED FILING JOINT OR WIDOW(ER)	$189,950		
5.	SUBTRACT LINE 4 FROM LINE 3		435,495.	
	IF LINE 5 IS MORE THAN $122,500 ($61,250 IF MARRIED FILING SEPARATE) ENTER ZERO ON FORM 1040, LINE 38.			
6.	DIVIDE LINE 5 BY $2,500 ($1,250 IF MFS) . .			
7.	MULTIPLY LINE 6 BY 2% (.02) AND ENTER THE RESULT AS A DECIMAL			
8.	MULTIPLY LINE 2 BY LINE 7			
9.	SUBTRACT LINE 8 FROM LINE 2. TOTAL TO FORM 1040, LINE 38.			0.

ROBERT L & SUSANNE D PIERCE [redacted]

FORM 1040	SEP DEDUCTION	STATEMENT 4
ROBERT L PIERCE		
1. PLAN CONTRIBUTION RATE OR SELF-EMPLOYED PERSON'S RATE		.130435
2. NET EARNINGS FROM SCHEDULE C, SCHEDULE F, OR SCHEDULE K-1		9,600.
3. DEDUCTION FOR SELF-EMPLOYMENT TAX FROM 1040, LINE 27		129.
4. SUBTRACT LINE 3 FROM LINE 2		9,471.
5. MULTIPLY LINE 4 TIMES LINE 1		1,235.
6. MULTIPLY $160,000 BY YOUR PLAN CONTRIBUTION RATE. ENTER THE RESULT BUT NOT MORE THAN $30,000		24,000.
7. ENTER THE SMALLER OF LINE 5 OR LINE 6 HERE AND INCLUDE IN THE TOTAL ON LINE 29, FORM 1040.		1,235.
SUSANNE D PIERCE		
1. PLAN CONTRIBUTION RATE OR SELF-EMPLOYED PERSON'S RATE		.130435
2. NET EARNINGS FROM SCHEDULE C, SCHEDULE F, OR SCHEDULE K-1		9,000.
3. DEDUCTION FOR SELF-EMPLOYMENT TAX FROM 1040, LINE 27		636.
4. SUBTRACT LINE 3 FROM LINE 2		8,364.
5. MULTIPLY LINE 4 TIMES LINE 1		1,091.
6. MULTIPLY $160,000 BY YOUR PLAN CONTRIBUTION RATE. ENTER THE RESULT BUT NOT MORE THAN $30,000		24,000.
7. ENTER THE SMALLER OF LINE 5 OR LINE 6 HERE AND INCLUDE IN THE TOTAL ON LINE 29, FORM 1040.		1,091.

FORM 1040	TAX-EXEMPT INTEREST	STATEMENT 5
NAME OF PAYER		AMOUNT
ED D JONES MUNI		1,239.
EDWARD D JONES		604.
MUNI BOND DIVIDENDS		34,680.
MUNI BOND DIVIDENDS		34,680.
TOTAL TO FORM 1040, LINE 8B		71,203.

ROBERT L & SUSANNE D PIERCE [redacted]

FORM 1040 WAGES RECEIVED AND TAXES WITHHELD STATEMENT 6

T S	EMPLOYER'S NAME	AMOUNT PAID	FEDERAL TAX WITHHELD	STATE TAX WITHHELD	CITY SDI TAX W/H	FICA TAX	MEDICARE TAX
T	HOME OIL & COAL COMPANY INC., SALISBURY, NC	107,582.	26,686.	7,379.		6,501.	1,685.
S	HOME OIL & COAL COMPANY INC., SALISBURY, NC	2,748.	265.	144.		186.	43.
T	CENTRAL CONCRETE, BURLINGTON, NC	37,119.	7,380.	2,640.		2,432.	569.
TOTALS		147,449.	34,311.	10,163.		7,119.	2,297.

DOJ-018255

ROBERT L & SUSANNE D PIERCE [redacted]

FORM 1040 EXCESS SOCIAL SECURITY TAX WORKSHEET STATEMENT 7

	TAXPAYER	SPOUSE
1. ADD ALL SOCIAL SECURITY TAX WITHHELD BUT NOT MORE THAN $4,501.20 FOR EACH EMPLOYER (THIS TAX SHOULD BE SHOWN IN BOX 4 OF YOUR W-2 FORMS). ENTER THE TOTAL HERE	6,933.	186.
2. ENTER ANY UNCOLLECTED SOCIAL SECURITY TAX ON TIPS OR GROUP-TERM LIFE INSURANCE INCLUDED IN THE TOTAL ON FORM 1040, LINE 56		
3. ADD LINES 1 AND 2	6,933.	186.
4. SOCIAL SECURITY TAX LIMIT	4,501.	4,501.
5. SUBTRACT LINE 4 FROM LINE 3. EXCESS SOCIAL SECURITY TAX INCLUDED IN FORM 1040, LINE 62	2,432.	0.

SCHEDULE A STATE AND LOCAL INCOME TAXES STATEMENT 8

DESCRIPTION	AMOUNT
HOME OIL & COAL COMPANY INC., SALISBURY, NC	7,379.
HOME OIL & COAL COMPANY INC., SALISBURY, NC	144.
CENTRAL CONCRETE, BURLINGTON, NC	2,640.
NORTH CAROLINA ESTIMATE PAYMENTS	104,200.
NORTH CAROLINA PRIOR YEAR BALANCE DUE AND EXTENSION PAYMENTS	3,787.
TOTAL TO SCHEDULE A, LINE 5	118,150.

SCHEDULE A CASH CONTRIBUTIONS STATEMENT 9

DESCRIPTION	AMOUNT 50% LIMIT	AMOUNT 30% LIMIT
MISCELLANEOUS	1,431.	
FROM K-1 - HOME OIL & COAL	571.	
FROM K-1 - ROBERT L PIERCE GRANTOR TRUST B	594.	
FROM K-1 - ROBERT L PIERCE GRANTOR TRUST A	594.	
SUBTOTALS	3,190.	
TOTAL TO SCHEDULE A, LINE 15		3,190.

ROBERT L & SUSANNE D PIERCE [redacted]

SCHEDULE A	MEDICAL AND DENTAL EXPENSES	STATEMENT 10
DESCRIPTION		AMOUNT
MEDICAL PAYMENTS PAID ON BEHALF 2% SHAREHOLDER FROM K-1 - HOME OIL & COAL		1,462.
TOTAL TO SCHEDULE A, LINE 1		1,462.

ROBERT L & SUSANNE D PIERCE [redacted]

SCHEDULE A	ITEMIZED DEDUCTIONS WORKSHEET		STATEMENT 11
1.	ADD THE AMOUNTS ON SCHEDULE A, LINES 4, 9, 14, 18, 19, 26, AND 27		137,584.
2.	ADD THE AMOUNTS ON SCHEDULE A, LINES 4, 13, AND 19, PLUS ANY GAMBLING AND CASUALTY OR THEFT LOSSES INCLUDED ON LINE 27		0.
3.	IS THE AMOUNT ON LINE 2 LESS THAN THE AMOUNT ON LINE 1? IF NO, YOUR DEDUCTION IS NOT LIMITED. ENTER THE AMOUNT FROM LINE 1 ABOVE ON SCHEDULE A, LINE 28. IF YES, SUBTRACT LINE 2 FROM LINE 1		137,584.
4.	MULTIPLY LINE 3 ABOVE BY 80% (.80)	110,067.	
5.	ENTER THE AMOUNT FROM FORM 1040, LINE 34	625,445.	
6.	ENTER: $126,600 IF SINGLE, MARRIED FILING JOINTLY, HEAD OF HOUSEHOLD, OR QUALIFYING WIDOW(ER); $63,300 IF MARRIED FILING SEPARATELY	126,600.	
7.	IS THE AMOUNT ON LINE 6 LESS THAN THE AMOUNT ON LINE 5? IF NO, YOUR DEDUCTION IS NOT LIMITED. ENTER THE AMOUNT FROM LINE 1 ABOVE ON SCHEDULE A, LINE 28. IF YES, SUBTRACT LINE 6 FROM LINE 5	498,845.	
8.	MULTIPLY LINE 7 ABOVE BY 3% (.03)	14,965.	
9.	ENTER THE SMALLER OF LINE 4 OR LINE 8		14,965.
10.	TOTAL ITEMIZED DEDUCTIONS. SUBTRACT LINE 9 FROM LINE 1. ENTER THE RESULT HERE AND ON SCHEDULE A, LINE 28		122,619.

SCHEDULE B	INTEREST INCOME	STATEMENT 12
NAME OF PAYER		AMOUNT
CCB		15,873.
CCB		256.
CCB		1,530.
EDWARD D JONES		99.
EQUITABLE LIFE		1,000.
PRUDENTIAL INS CO		116.
CCB-NOMINEE ACCOUNT		45.
CCB-NOMINEE ACCOUNT		13.
ST ALEX BROWN (SALISBURY INVESTMENTS)		<9.>
FROM K-1 - DAVIDSON DIV R/E III,		982.
FROM K-1 - ROWE OIL & COAL		4.
FROM K-1 - PIERCE INVESTMENTS INC		15,822.
FROM K-1 - ROWE CONCRETE & SUPPLY LLC		788.
FROM K-1 - ROBERT L PIERCE GRANTOR TRUST B		1.
FROM K-1 - ROBERT L PIERCE GRANTOR TRUST A		16,487.
		16,485.

ROBERT L & SUSANNE D PIERCE [redacted]

FROM K-1 - HOME OIL & COAL	<29,956.>
FROM K-1 - HOME CONCRETE & SUPPLY LLC	<5.>
US OBLIGATIONS	15,168.
U S OBLIGATIONS	15,168.
TOTAL TO SCHEDULE B, LINE 1	69,327.

SCHEDULE B — DIVIDEND INCOME — STATEMENT 13

NAME OF PAYER	AMOUNT
BANKAMERICA CORP	12,506.
CCB FINANCIAL CORP	45,199.
CCB FINANCIAL CORP	83.
EDWARD D JONES	1,257.
EDWARD D JONES	764.
EDWARD D JONES	1,090.
F&M FINANCIAL CORP	130.
F&M FINANCIAL CORP	130.
FOOD LION A	4,060.
FOOD LION A	4,060.
FOOD LION B	3,998.
FOOD LION B	1,839.
CHARLES SCHWAB & CO	250.
INNES STREET FINANCIAL CORP	86.
DELHAIZE AMERICA B	253.
DELHAIZE AMERICA B	1,333.
DELHAIZE AMERICA A	1,353.
DELHAIZE AMERICA A	1,353.
BT ALEX BROWN (SALISBURY INVESTMENTS)	3.
FROM K-1 - RO-BUCK MUTUAL INVESTMENT CLUB	79.
FROM K-1 - ROBERT L PIERCE GRANTOR TRUST B	1,605.
FROM K-1 - ROBERT L PIERCE GRANTOR TRUST A	1,650.
MUNI BOND DIVIDENDS	34,680.
MUNI BOND DIVIDENDS	34,680.
TOTAL TO SCHEDULE B, LINE 5	152,441.

SCHEDULE B — TAX-EXEMPT INTEREST FROM 1099-DIV — STATEMENT 14

NAME OF PAYER	AMOUNT
EDWARD D JONES	604.
MUNI BOND DIVIDENDS	34,680.
MUNI BOND DIVIDENDS	34,680.
TOTAL TAX-EXEMPT INTEREST FROM 1099-DIV TO SCHEDULE B, LINE 5	69,964.

Case 7:06-cv-00181-FL Document 26-4 Filed 04/19/07 Page 27 of 31
DOJ-018259

ROBERT L & SUSANNE D PIERCE [redacted]

SCHEDULE C-EZ	GROSS RECEIPTS	STATEMENT 15
DESCRIPTION		AMOUNT
HOME OIL & COAL COMPANY DIRECTOR FEES		9,000.
CENTRAL CAROLINA BANK DIRECTOR FEES		600.
TOTAL TO SCHEDULE C-EZ, LINE 1		9,600.

SCHEDULE C-EZ	GROSS RECEIPTS	STATEMENT 16
DESCRIPTION		AMOUNT
HOME OIL & COAL COMPANY DIRECTORS FEE		9,000.
TOTAL TO SCHEDULE C-EZ, LINE 1		9,000.

SCHEDULE D	NET LONG-TERM GAIN OR LOSS FROM FORMS 4797, 2439, 6252, 4684, 6781 AND 8824		STATEMENT 17
DESCRIPTION OF PROPERTY		GAIN OR LOSS	28% GAIN
FORM 4797		6,178.	
TOTAL TO SCHEDULE D, PART II, LINE 11		6,178.	

SCHEDULE D	NET SHORT-TERM GAIN OR LOSS FROM PARTNERSHIPS, S CORPORATIONS, AND FIDUCIARIES	STATEMENT 18
DESCRIPTION OF ACTIVITY		GAIN OR LOSS
HOME OIL & COAL		29,734.
HOME CONCRETE & SUPPLY LLC		5.
ROBERT L PIERCE GRANTOR TRUST B		31,116.
ROBERT L PIERCE GRANTOR TRUST A		31,116.
TOTAL TO SCHEDULE D, PART I, LINE 5		91,971.

ROBERT L & SUSANNE D PIERCE [redacted]

SCHEDULE D — NET LONG-TERM GAIN OR LOSS FROM PARTNERSHIPS, S CORPORATIONS, AND FIDUCIARIES — STATEMENT 19

DESCRIPTION OF ACTIVITY	GAIN OR LOSS	28% GAIN
HOME OIL & COAL	<42,425.>	
PIERCE INVESTMENTS INC	27,000.	
RO-BUCK MUTUAL INVESTMENT CLUB	<52.>	
HOME CONCRETE & SUPPLY LLC	<8.>	
ROBERT L PIERCE GRANTOR TRUST B	<44,397.>	
ROBERT L PIERCE GRANTOR TRUST A	<44,397.>	
TOTAL TO SCHEDULE D, PART II, LINE 12	<104,279.>	

SCHEDULE D — CAPITAL GAIN DISTRIBUTIONS — STATEMENT 20

NAME OF PAYER	TOTAL CAPITAL GAIN	28% GAIN
EDWARD D JONES	902.	
TOTALS TO SCHEDULE D, LINE 13	902.	

ROBERT L & SUSANNE D PIERCE [redacted]

SCHEDULE D — CAPITAL LOSS CARRYOVER — STATEMENT 21

1.	ENTER THE AMOUNT FROM FORM 1040, LINE 37	502,826.
2.	ENTER THE LOSS FROM SCHEDULE D, LINE 18, AS A POSITIVE AMOUNT.	3,000.
3.	COMBINE LINES 1 AND 2. IF ZERO OR LESS, ENTER -0-	505,826.
4.	ENTER THE SMALLER OF LINE 2 OR LINE 3	3,000.
5.	ENTER THE LOSS FROM SCHEDULE D, LINE 7, AS A POSITIVE AMOUNT	
6.	ENTER THE GAIN, IF ANY, FROM SCHEDULE D, LINE 16	
7.	ADD LINES 4 AND 6	
8.	SHORT-TERM CAPITAL LOSS CARRYOVER TO 2000. SUBTRACT LINE 7 FROM LINE 5. IF ZERO OR LESS, ENTER -0-	
9.	ENTER THE LOSS FROM SCHEDULE D, LINE 16, AS A POSITIVE AMOUNT.	113,322.
10.	ENTER THE GAIN, IF ANY, FROM SCHEDULE D, LINE 7 — 91,971.	
11.	SUBTRACT LINE 5 FROM LINE 4. IF ZERO OR LESS, ENTER -0- — 3,000.	
12.	ADD LINES 10 AND 11	94,971.
13.	LONG-TERM CAPITAL LOSS CARRYOVER TO 2000. SUBTRACT LINE 12 FROM LINE 9. IF ZERO OR LESS, ENTER -0-	18,351.

SCHEDULE D — ALTERNATIVE MINIMUM TAX — STATEMENT 22

NET LONG-TERM GAIN OR LOSS FROM PARTNERSHIPS, S CORPORATIONS, ESTATES AND TRUSTS

DESCRIPTION OF ACTIVITY	GAIN OR LOSS	28% GAIN
HOME OIL & COAL	<42,425.>	
PIERCE INVESTMENTS INC	27,000.	
RO-BUCK MUTUAL INVESTMENT CLUB	<52.>	
HOME CONCRETE & SUPPLY LLC	<8.>	
ROBERT L PIERCE GRANTOR TRUST B	<44,397.>	
ROBERT L PIERCE GRANTOR TRUST A	<44,397.>	
TOTAL TO SCHEDULE D, PART II, LINE 12	<104,279.>	

ROBERT L & SUSANNE D PIERCE [redacted]

SCHEDULE D — ALTERNATIVE MINIMUM TAX — CAPITAL GAIN DISTRIBUTIONS — STATEMENT 23

NAME OF PAYER	TOTAL CAPITAL GAIN	28% GAIN
EDWARD D JONES	902.	
TOTALS TO SCHEDULE D, LINE 13	902.	

SCHEDULE D — ALTERNATIVE MINIMUM TAX — NET LONG-TERM GAIN OR LOSS FROM FORMS 4797, 2439, 6252, 4684, 6781 AND 8824 — STATEMENT 24

DESCRIPTION OF PROPERTY	GAIN OR LOSS	28% GAIN
FORM 4797 AMT	6,178.	
TOTAL TO SCHEDULE D, PART II, LINE 11	6,178.	

SCHEDULE D — ALTERNATIVE MINIMUM TAX — NET SHORT-TERM GAIN OR LOSS FROM PARTNERSHIPS, S CORPORATIONS, ESTATES AND TRUSTS — STATEMENT 25

DESCRIPTION OF ACTIVITY	GAIN OR LOSS
HOME OIL & COAL	29,734.
HOME CONCRETE & SUPPLY LLC	5.
ROBERT L PIERCE GRANTOR TRUST B	31,116.
ROBERT L PIERCE GRANTOR TRUST A	31,116.
TOTAL TO SCHEDULE D, PART I, LINE 5	91,971.

ROBERT L & SUSANNE D PIERCE [redacted]

SCHEDULE D — ALTERNATIVE MINIMUM TAX CAPITAL LOSS CARRYOVER — STATEMENT 26

1. ENTER THE AMOUNT FROM FORM 6251, LINE 21		100,602.
2. ENTER THE LOSS FROM SCH D, LINE 18, AS A POSITIVE AMOUNT		3,000.
3. COMBINE LINES 1 AND 2. IF ZERO OR LESS, ENTER -0-		103,602.
4. ENTER THE SMALLER OF LINE 2 OR LINE 3		3,000.
5. ENTER THE LOSS FROM SCH D, LINE 7, AS A POSITIVE AMOUNT		
6. ENTER THE GAIN, IF ANY, FROM SCHEDULE D, LINE 16		
7. ADD LINES 4 AND 6		
8. SHORT-TERM CAPITAL LOSS CARRYOVER TO 2000. SUBTRACT LINE 7 FROM LINE 5. IF ZERO OR LESS, ENTER -0-		
9. ENTER THE LOSS FROM SCH D, LINE 16, AS A POSITIVE AMOUNT		113,284.
10. ENTER THE GAIN, IF ANY, FROM SCHEDULE D, LINE 7	91,971.	
11. SUBTRACT LINE 5 FROM LINE 4. IF ZERO OR LESS, ENTER -0-	3,000.	
12. ADD LINES 10 AND 11		94,971.
13. LONG-TERM CAPITAL LOSS CARRYOVER TO 2000. SUBTRACT LINE 12 FROM LINE 9. IF ZERO OR LESS, ENTER -0-		18,313.

SCHEDULE E — INCOME OR (LOSS) FROM PARTNERSHIPS AND S CORPS — STATEMENT 27

NAME

EMPLOYER ID NO.	NOT AT RISK	X IF FRN	CODE	PASSIVE LOSS	PASSIVE INCOME	NONPASSIVE LOSS	SEC. 179 DEDUCTION	NONPASSIVE INCOME
DAVIDSON DIV R/E III, 62-1242599	X		P	170.				
ROBE OIL & COAL 56-0566791			S					119,492.
PIERCE INVESTMENTS INC 56-1724599			S		5,119.			
RO-BUCK MUTUAL INVESTMENT CLUB 56-6098439			P					1.
ROBE CONCRETE & SUPPLY LLC			P	37.				
ROBERT L PIERCE GRANTOR TRUST B 58-6300593			P			1,293.		
ROBERT L PIERCE GRANTOR TRUST B 58-6300593			S					126,297.
ROBERT L PIERCE GRANTOR TRUST A 58-6300592			P			1,293.		

Case 7:06-cv-00181-FL Document 26-5 Filed 04/19/07 Page 1 of 3 DOJ-018264

ROBERT L & SUSANNE D PIERCE [redacted]

ROBERT L PIERCE GRANTOR TRUST A 58-6388592 E					124,297.
TOTALS TO SCH. E, LN. 28	207.	5,119.	2,586.		368,087.

SCHEDULE SE	NON-FARM INCOME	STATEMENT 28
DESCRIPTION		AMOUNT
FROM SCHEDULE C		9,000.
TOTAL TO SCHEDULE SE, LINE 2		9,000.

SCHEDULE SE	NON-FARM INCOME	STATEMENT 29
DESCRIPTION		AMOUNT
FROM SCHEDULE C		9,600.
TOTAL TO SCHEDULE SE, LINE 2		9,600.

FORM 6198	DECREASES IN BASIS	STATEMENT 30

DAVIDSON DIV R/E III,

DESCRIPTION	AMOUNT
ASSETS WITHDRAWN FROM ACTIVITY	3.
TOTAL TO FORM 6198, LINE 5 OR LINE 16	3.

Transferor's Statement under
Reg 1.351-3(b)
Robert L Pierce
SSN [redacted]
From 1040, Tax Year Ending 12/31/1999

1. Description of property transferred.
Property transferred by Robert L. Pierce June 16, 1999

Property
.0100% interest in Home Connector Supply LLC EIN 56-2136387

2. Cost or basis in hands of transferor as of date of transfer
Robert L. Pierce $ 66,891.14

3. i. Total issued and outstanding capital stock immediately prior to the exchange 9,300

ii. Total issued and outstanding capital stock immediately after the exchange 9,300

iii. Stock issued in the exchange None

Shares owned by transferor immediately prior to and after the exchange

Robert L. Pierce 43

iii. Fair market value of stock issued to transferor Not applicable

4. i. Principal amount and terms of all securities outstanding immediately prior to and immediately after the exchange Not applicable

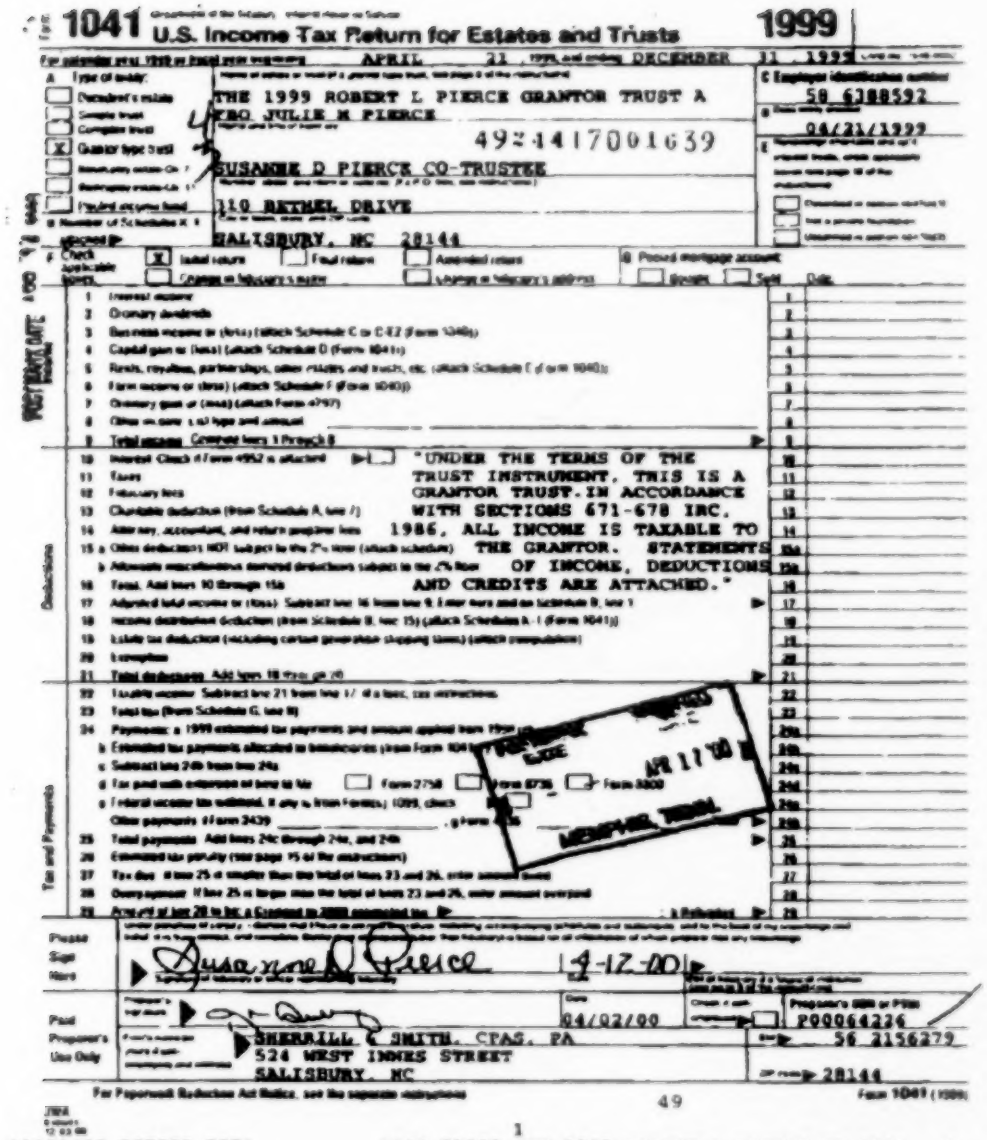
ii. Principal amount and terms of all securities issued to transferors in the exchange and the transferor's holdings of securities immediately prior to and immediately after the exchange Not applicable

iii. Fair market value of securities issued to transferor Not applicable

5. Amount of money passed to transferors None

6. Other property which was passed to transferors None

7. Liabilities assumed by the controlled corporation in the exchange None



Form 1041 U.S. Income Tax Return for Estates and Trusts 1999

For calendar year 1999 or fiscal year beginning APRIL 21, 1999, and ending DECEMBER 31, 1999

A Type of entity:
- [ ] Decedent's estate
- [ ] Simple trust
- [ ] Complex trust
- [X] Qualified type trust
- [ ] Bankruptcy estate-Ch. 7
- [ ] Bankruptcy estate-Ch. 11
- [ ] Pooled income fund

B Number of Schedules K-1 attached ▶

THE 1999 ROBERT L PIERCE GRANTOR TRUST A
FBO JULIE M PIERCE
4924417001639
SUSANNE D PIERCE CO-TRUSTEE
110 BETHEL DRIVE
SALISBURY, NC 28144

C Employer identification number: 58 6388592

D Date entity created: 04/21/1999

E Nonexempt charitable and split-interest trusts, check applicable boxes
- [ ] Check if a private foundation
- [ ] Check if filing under section 1563(e)(3)(C)

F Check applicable boxes: [X] Initial return [ ] Final return [ ] Amended return [ ] Change in fiduciary's name [ ] Change in fiduciary's address

G Pooled mortgage account: [ ] Yes [ ] No

Income	1	Interest income	1
	2	Ordinary dividends	2
	3	Business income or (loss) (attach Schedule C or C-EZ (Form 1040))	3
	4	Capital gain or (loss) (attach Schedule D (Form 1041))	4
	5	Rents, royalties, partnerships, other estates and trusts, etc. (attach Schedule E (Form 1040))	5
	6	Farm income or (loss) (attach Schedule F (Form 1040))	6
	7	Ordinary gain or (loss) (attach Form 4797)	7
	8	Other income. List type and amount	8
	9	Total income. Combine lines 1 through 8 ▶	9
Deductions	10	Interest. Check if Form 4952 is attached ▶[ ]	10
	11	Taxes	11
	12	Fiduciary fees	12
	13	Charitable deduction (from Schedule A, line 7)	13
	14	Attorney, accountant, and return preparer fees	14
	15a	Other deductions NOT subject to the 2% limit (attach schedule)	15a
	b	Allowable miscellaneous itemized deductions subject to the 2% limit	15b
	16	Total. Add lines 10 through 15b	16
	17	Adjusted total income or (loss). Subtract line 16 from line 9. Enter here and on Schedule B, line 1 ▶	17
	18	Income distribution deduction (from Schedule B, line 15) (attach Schedules A and B (Form 1041))	18
	19	Estate tax deduction (including certain generation-skipping taxes) (attach computation)	19
	20	Exemption	20
	21	Total deductions. Add lines 18 through 20 ▶	21
Tax and Payments	22	Taxable income. Subtract line 21 from line 17. If a loss, see instructions	22
	23	Total tax (from Schedule G, line 8)	23
	24a	Payments: a 1999 estimated tax payments and amount applied from 1998 return	24a
	b	Estimated tax payments allocated to beneficiaries (from Form 1041-T)	24b
	c	Subtract line 24b from line 24a	24c
	d	Tax paid with extension of time to file: [ ] Form 2758 [ ] Form 8736 [ ] Form 8800	24d
	e	Federal income tax withheld. If any, is from Forms: 1099, check ▶[ ]	24e
		Other payments: f Form 2439 _____ g Form 4136 _____	24f, 24g
	25	Total payments. Add lines 24c through 24g, and 24h	25
	26	Estimated tax penalty (see page 15 of the instructions)	26
	27	Tax due. If line 25 is smaller than the total of lines 23 and 26, enter amount owed	27
	28	Overpayment. If line 25 is larger than the total of lines 23 and 26, enter amount overpaid	28
	29	Amount of line 28 to be: a Credited to 2000 estimated tax ▶ b Refunded ▶	29a, 29b

RECEIVED APR 17 '00 OGDEN MEMPHIS, TENN.

Please Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than fiduciary) is based on all information of which preparer has any knowledge.

Susanne D Pierce 4-17-00 ▶
Signature of officer or fiduciary — Date

Paid Preparer's Use Only

Preparer's signature ▶ Date 04/02/00 Check if self-employed ▶[ ] Preparer's SSN or PTIN P00064236

Firm's name (or yours if self-employed) and address ▶ SHERRILL C SMITH, CPAS, PA
524 WEST INNES STREET
SALISBURY, NC
Firm's EIN ▶ 56 2156279
ZIP code ▶ 28144

For Paperwork Reduction Act Notice, see the separate instructions. 49 Form 1041 (1999)

JWA 12 03 99

1
09200402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 1

THE 1999 ROBERT L PIERCE GRANTOR TRUST A 58-6188592

Schedule A | Charitable Deduction. Do not complete for a simple trust or a grantor trust.

1 Amounts paid or permanently set aside for charitable purposes from gross income (see instructions) 1
2 Tax-exempt income allocable to charitable contributions (see instructions) 2
3 Subtract line 2 from line 1 3
4 Capital gains for the tax year allocated to corpus and paid or permanently set aside for charitable purposes 4
5 Add lines 3 and 4 5
6 Section 1202 exclusion allocable to capital gains paid or permanently set aside for charitable purposes (see instructions) 6
7 Charitable deduction. Subtract line 6 from line 5. Enter here and on page 1, line 13 7

Schedule B | Income Distribution Deduction

1 Adjusted total income (loss) (see instructions) 1
2 Adjusted tax-exempt interest 2
3 Total net gain from Schedule D (Form 1041), line 15, column (1) (see instructions) 3
4 Enter amount from Schedule A, line 4 (reduced by any allocable section 1202 exclusion) 4
5 Capital gains for the tax year included on Schedule A, line 1 (see instructions) 5
6 Enter any gain from page 1, line 4, as a negative number. If page 1, line 4, is a loss, enter the loss as a positive number 6
7 Distributable net income (DNI). Combine lines 1 through 6. If zero or less, enter -0- 7
8 If a complex trust, enter accounting income for the tax year as determined under the governing instrument and applicable local law 8
9 Income required to be distributed currently 9
10 Other amounts paid, credited, or otherwise required to be distributed 10
11 Total distributions. Add lines 9 and 10. If greater than line 8, see instructions 11
12 Enter the amount of tax-exempt income included on line 11 12
13 Tentative income distribution deduction. Subtract line 12 from line 11 13
14 Tentative income distribution deduction. Subtract line 7 from line 7. If zero or less, enter -0- 14
15 Income distribution deduction. Enter the smaller of line 13 or line 14 here and on page 1, line 18 15

Schedule G | Tax Computation

1 Tax: a ☐ Tax rate schedule or ☐ Schedule D (Form 1041) 1a
b Tax on lump-sum distributions (attach Form 4972) 1b
c Total. Add lines 1a and 1b 1c
2a Foreign tax credit (attach Form 1116) 2a
b Check ☐ if recomputed using look-back method ☐ Form 8834 2b
c General business credit. Enter here and check which forms are attached ☐ Form 3800 or ☐ Form (specify) ▶ 2c
d Credit for prior year minimum tax (attach Form 8801) 2d
3 Total credits. Add lines 2a through 2d 3
4 Subtract line 3 from line 1c 4
5 Recapture taxes. Check if from: ☐ Form 4255 ☐ Form 8611 5
6 Alternative minimum tax (from Schedule I, line 39) 6
7 Household employment taxes. Attach Schedule H (Form 1040) 7
8 Total tax. Add lines 4 through 7. Enter here and on page 1, line 23 8

Other Information

		Yes	No
1	Did the estate or trust receive tax-exempt income? If "Yes," attach a computation of the allocation of expenses. Enter the amount of tax-exempt interest income and exempt-interest dividends ▶ $ 34,680.	X	
2	Did the estate or trust receive all or any part of the earnings (salary, wages, and other compensation) of any individual by reason of a contract assignment or similar arrangement?		X
3	At any time during calendar year 1999, did the estate or trust have an interest in or a signature or other authority over a bank, securities, or other financial account in a foreign country? See the instructions for exceptions and filing requirements for Form TD F 90-22.1. If "Yes," enter the name of the foreign country ▶		X
4	During the tax year, did the estate or trust receive a distribution from, or was it the grantor of, or transferor to, a foreign trust? If "Yes," the estate or trust may have to file Form 3520. See instructions		X
5	Did the estate or trust receive, or pay, any qualified residence interest on seller-provided financing? If "Yes," see page 19 for required attachment		X
6	If this is an estate or a complex trust making the section 663(b) election, check here ▶ ☐		
7	To make a section 643(e)(3) election, attach Schedule D (Form 1041), and check here ▶ ☐		
8	If the decedent's estate has been open for more than 2 years, attach an explanation for the delay in closing the estate, and check here ▶ ☐		
9	Are any shares of Liquid Gold Services (the parent) Sec instructions		X

Form 1041 (99)

09200402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 1

GRANTOR LETTER

SUSANNE D PIERCE CO-TRUSTEE
310 BETHEL DRIVE
SALISBURY, NC 28144

As Year Ended: 12/31/99

Grantor Name & Address	Name of Trust
ROBERT L PIERCE 310 BETHEL DRIVE SALISBURY, NC 28144	THE 1999 ROBERT L PIERCE GRANTOR TRUS FBO JULIE M PIERCE
Social Security Number: [redacted]	Employer ID Number 58-6388592

THE FOLLOWING INCOME, DEDUCTIONS AND CREDITS ARE TO BE REPORTED ON THE INCOME TAX RETURNS FOR THE ABOVE NAMED GRANTOR, IF REQUIRED.

FEDERAL INFORMATION	
INCOME	
INTEREST INCOME..... (ENTER ON FORM 1040, SCHEDULE B, PART I, LINE 1)	16,485.
INTEREST FROM U.S. OBLIGATIONS NOT INCLUDED ELSEWHERE..... (ENTER ON FORM 1040, SCHEDULE B, PART I, LINE 1)	15,168.
DIVIDEND INCOME..... (ENTER ON FORM 1040, SCHEDULE B, PART II, LINE 5)	1,650.
NONPASSIVE INCOME (LOSS) FROM PARTNERSHIPS..... (ENTER ON FORM 1040, SCHEDULE E, PART II)	<1,293.
NONPASSIVE INCOME (LOSS) FROM S CORPORATIONS..... (ENTER ON FORM 1040, SCHEDULE E, PART II)	124,297.
SHORT-TERM GAIN (LOSS) FROM PARTNR, S CORPS & FIDUCIARIES.. (ENTER ON FORM 1040, SCHEDULE D, PART I)	31,116.
LONG-TERM GAIN (LOSS) FROM PARTNR, S CORPS & FIDUCIARIES... 28% RATE GAIN (LOSS) INCLUDED IN AMOUNT ABOVE..... (ENTER ON FORM 1040, SCHEDULE D, PART II)	<44,397. 0.
ORDINARY GAIN (LOSS)..... (ENTER ON FORM 4797, PART II)	<30,417.
DEDUCTIONS	
CHARITABLE DEDUCTION..... (ENTER ON FORM 1040, SCHEDULE A, LINE 15)	594.
TAX PREFERENCES	
DEPRECIATION ADJUSTMENT FOR POST 1986 PROPERTY..... (ENTER ON FORM 6251, LINE 8)	2,390.
ADJUSTED GAIN OR LOSS.....	<175,078.

GRANTOR NAME: ROBERT L PIERCE

SOC. SEC. NUMBER: [redacted]

(ENTER ON FORM 6251, LINE 9)

TAX-EXEMPT

MUNICIPAL TAX-EXEMPT INTEREST
(ENTER ON FORM 1040, LINE 8B)

NORTH CAROLINA TAX-EXEMPT INTEREST..... 34,680.

NORTH CAROLINA INFORMATION

SUBTRACTIONS

INTEREST ON U.S. OBLIGATIONS..... 15,168.
(ENTER ON FORM D-400, LINE 42)

CREDITS AND TAXES

OTHER CREDITS..... 246.
(ENTER ON FORM D-400TC, PART 4, LINE 25)

SCHEDULE E (Form 1040)

Supplemental Income and Loss

(From rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.)

1999

▶ Attach to Form 1040 or Form 1041. ▶ See instructions for Schedule E (Form 1040).

Attachment Sequence No. 13

Name(s) shown on return

THE 1999 ROBERT L PIERCE GRANTOR TRUST A
FBO JULIE K PIERCE

Your social security number

58-6388592

Part I Income or Loss From Rental Real Estate and Royalties Note: Report income and expenses from your business of renting personal property on Schedule C or C-EZ. Report farm rental income or loss from Form 4835 on page 2, line 39.

1 Show the kind and location of each rental real estate property:

A
B
C

2 For each rental real estate property listed on line 1, did you or your family use it during the tax year for personal purposes for more than the greater of:
- 14 days, or
- 10% of the total days rented at fair rental value?
(See page E-1.)

	Yes	No
A		
B		
C		

Income:		Properties A	Properties B	Properties C	Totals (Add columns A, B, and C.)
3 Rents received	3				3
4 Royalties received	4				4
Expenses:					
5 Advertising	5				
6 Auto and travel (see page E-2)	6				
7 Cleaning and maintenance	7				
8 Commissions	8				
9 Insurance	9				
10 Legal and other professional fees	10				
11 Management fees	11				
12 Mortgage interest paid to banks, etc. (see page E-2)	12				12
13 Other interest	13				
14 Repairs	14				
15 Supplies	15				
16 Taxes	16				
17 Utilities	17				
18 Other (list) ▶	18				
19 Add lines 5 through 18	19				19
20 Depreciation expense or depletion (see page E-3)	20				20
21 Total expenses. Add lines 19 and 20	21				
22 Income or (loss) from rental real estate or royalty properties. Subtract line 21 from line 3 (rents) or line 4 (royalties). If the result is a (loss), see page E-3 to find out if you must file Form 6198	22				
23 Deductible rental real estate loss. Caution: Your rental real estate loss on line 22 may be limited. See page E-3 to find out if you must file Form 8582. Real estate professionals must complete line 42 on page 2	23				
24 Income. Add positive amounts shown on line 22. Do not include any losses					24
25 Losses. Add royalty losses from line 22 and rental real estate losses from line 23. Enter the total losses here					25 ( )
26 Total rental real estate and royalty income or (loss). Combine lines 24 and 25. Enter the result here. If Parts II, III, IV, and line 39 on page 2 do not apply to you, also enter this amount on Form 1040, line 17. Otherwise, include this amount in the total on line 40 on page 2					26 0.

For Paperwork Reduction Act Notice, see Form 1040 Instructions. 5 Schedule E (Form 1040) 1999

09200402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 1

Schedule E (Form 1040) 2000 — Attachment Sequence No. 13 — Page 2

THE 1999 ROBERT L PIERCE GRANTOR TRUST A
FBO JULIE M PIERCE

Your social security number: 58-6388592

Note: If you report amounts from farming or fishing on Schedule E, you must enter your gross income from those activities on line 41 below.
Real estate professionals must complete line 42 below.

Part II Income or Loss From Partnerships and S Corporations Note. If you report a loss from an at-risk activity, you MUST check either column (e) or (f) on line 27 to describe your investment in the activity. If you check column (f), you must attach Form 6198.

27	(a) Name	(b) Enter P for partnership; S for S corporation	(c) Check if foreign partnership	(d) Employer identification number	(e) All is investment at risk	(f) Some is not at risk
A	HOME OIL & COAL INC	S		56-0546791	X	
B	HOME CONCRETE & SUPPLY, LLC	P		56-2136387	X	
C						
D						
E						

	Passive Income and Loss			Nonpassive Income and Loss	
	(g) Passive loss allowed (attach Form 8582 if required)	(h) Passive income from Schedule K-1	(i) Nonpassive loss from Schedule K-1	(j) Section 179 expense deduction from Form 4562	(k) Nonpassive income from Schedule K-1
A					124,297.
B			1,293.		
C					
D					
E					
28a	Totals				124,297.
b	Totals		1,293.		
29	Add columns (h) and (k) of line 28a				29 124,297.
30	Add columns (g), (i), and (j) of line 28b				30 (1,293.)
31	Total partnership and S corporation income or (loss). Combine lines 29 and 30. Enter the result here and include in the total on line 40 below				31 123,004.

Part III Income or Loss From Estates and Trusts

32	(a) Name	(b) Employer identification number
A		
B		

	Passive Income and Loss		Nonpassive Income and Loss	
	(c) Passive deduction or loss allowed (attach Form 8582 if required)	(d) Passive income from Schedule K-1	(e) Deduction or loss from Schedule K-1	(f) Other income from Schedule K-1
A				
B				
33a	Totals			
b	Totals			
34	Add columns (d) and (f) of line 33a			34
35	Add columns (c) and (e) of line 33b			35 ( )
36	Total estate and trust income or (loss). Combine lines 34 and 35. Enter the result here and include in the total on line 40 below			36

Part IV Income or Loss From Real Estate Mortgage Investment Conduits (REMICs) - Residual Holder

37	(a) Name	(b) Employer identification number	(c) Excess inclusion from Schedules Q, line 2c	(d) Taxable income (net loss) from Schedules Q, line 1b	(e) Income from Schedules Q, line 3b

38 Combine columns (d) and (e) only. Enter the result here and include in the total on line 40 below — 38

Part V Summary

39	Net farm rental income or (loss) from Form 4835. Also, complete line 41 below	39	
40	TOTAL income or (loss). Combine lines 26, 31, 36, 38, and 39. Enter the result here and on Form 1040, line 17	40	123,004.
41	Reconciliation of Farming and Fishing Income. Enter your gross farming and fishing income reported on Form 4835, line 7; Schedule K-1 (Form 1065), line 15b; Schedule K-1 (Form 1120S), line 23; and Schedule K-1 (Form 1041), line 14 (see page E-6)	41	
42	Reconciliation for Real Estate Professionals. If you were a real estate professional, enter the net income or (loss) you reported anywhere on Form 1040 from all rental real estate activities in which you materially participated under the passive activity loss rules	42	

Schedule E (Form 1040) 2000

09200402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 1

DOJ-018307

1999 Income from Passthroughs

HOME OIL & COAL INC
I.D. NUMBER: 56-0546791
TYPE: S CORPORATION

ACTIVITY INFORMATION:

HOME OIL & COAL INC

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	124,297
SCHEDULE E ACTIVITY INCOME (LOSS)	124,297

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1	.056
ADJUSTED GAIN OR LOSS	.033

OTHER K-1 INFORMATION:

INTEREST - TOTAL	.458
SHORT-TERM CAPITAL GAIN (LOSS)	.930
LONG-TERM CAPITAL GAIN (LOSS)	.131
CONTRIBUTIONS	594
SECTION 1231 GAIN (LOSS)	.236

Pierce
F 1040
Sch E
Stmt 29
(124, 297)

DOJ-018308

1999 Income from Passthroughs

HOME CONCRETE & SUPPLY, LLC
I.D. NUMBER: 56-2136367
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

HOME CONCRETE & SUPPLY, LLC

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	-1,293	
SCHEDULE E ACTIVITY INCOME (LOSS)		-1,293

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	334
ADJUSTED GAIN OR LOSS	-1,045

OTHER K-1 INFORMATION:

INTEREST - TOTAL	27
SHORT-TERM CAPITAL GAIN (LOSS)	186
LONG-TERM CAPITAL GAIN (LOSS)	-266
SECTION 1231 GAIN (LOSS)	-181

1999 Income from Passthroughs

SUMMARY OF K-1 INFORMATION FOR ALL PASSTHROUGHS

OTHER K-1 INFORMATION:

INTEREST - TOTAL	16,485
SHORT-TERM CAPITAL GAIN (LOSS)	31,116
LONG-TERM CAPITAL GAIN (LOSS)	-44,397
SECTION 1231 GAIN (LOSS)	-30,417

DEDUCTIONS:

CONTRIBUTIONS	594

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	2,390
ADJUSTED GAIN OR LOSS	-175,078

DOJ-018310

Form **4797** — Sales of Business Property (Also Involuntary Conversions and Recapture Amounts Under Sections 179 and 280F(b)(2)) — **1999**

THE 1999 ROBERT L PIERCE GRANTOR TRUST A
FBO JULIE M PIERCE

58-6388592

1 Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-S (or a substitute statement) that you will be including on line 2, 10, or 20 — 1

Part I Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft - Property Held More Than 1 Year

(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
HOME OIL & COAL INC						<30,236.>
HOME CONCRETE & SUPPLY, LLC						<181.>

3	Gain, if any, from Form 4684, line 39	3
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5
6	Gain, if any, from line 32, from other than casualty or theft	6
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows: Partnerships (except electing large partnerships). Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 9. Skip lines 8, 9, 11, and 12 below. S corporations. Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax. All others. If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	7	<30,417.>
8	Nonrecaptured net section 1231 losses from prior years	8	
9	Subtract line 8 from line 7. If zero or less, enter -0-. Also enter on the appropriate line as follows: S corporations. Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below. All others. If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below and enter the gain from line 9 as a long-term capital gain on Schedule D	9	

Part II Ordinary Gains and Losses

10	Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):					
11	Loss, if any, from line 7				11	<30,417.>
12	Gain, if any, from line 7, or amount from line 8, if applicable				12	
13	Gain, if any, from line 31				13	
14	Net gain or (loss) from Form 4684, lines 31 and 38b				14	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36				15	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824				16	
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations				17	
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:				18	<30,417.>
a	For all except individual returns: Enter the gain or (loss) from line 18 on the return being filed.					
b	For individual returns: (1) If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)."	18b(1)				
	(2) Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)				<30,417.>

LHA For Paperwork Reduction Act Notice, see separate instructions. Form 4797 (1999)

09200402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 1

DOJ-018311

Form 4797 (1999) PRO JULIE M PIERCE 58 6388592 Page 2

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255

19a (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A		
B		
C		
D		

These columns relate to the properties on lines 19A through 19D.		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20				
21 Cost or other basis plus expense of sale	21				
22 Depreciation (or depletion) allowed or allowable	22				
23 Adjusted basis. Subtract line 22 from line 21	23				
24 Total gain. Subtract line 23 from line 20	24				
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a				
b Enter the smaller of line 24 or 25a	25b				
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation	34		
35 Recapture amount. Subtract line 34 from line 33	35		

Form 4797 (1999)

09200402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251___1

THE 1999 ROBERT L PIERCE GRANTOR TRUST A 58-6388592

FORM 1041 INTEREST STATEMENT 1

DESCRIPTION	U.S. INTEREST	OTHER TAXABLE INTEREST
BT ALEX BROWN INC	46,515.	
HOME OIL & COAL, INC.	<31,160.>	
HOME CONCRETE & SUPPLY LLC	<187.>	
HOME OIL & COAL INC - REGULAR INTEREST		16,458.
HOME CONCRETE & SUPPLY, LLC - REGULAR INTEREST		27.
SUBTOTALS	15,168.	16,485.
TOTAL TO GRANTOR LETTER		31,653.

FORM 1041 DIVIDENDS STATEMENT 2

DESCRIPTION	U.S. INTEREST	REGULAR DIVIDENDS
CHARLES SCHWAB & CO INC		1,494.
BT ALEX BROWN		156.
SUBTOTALS		1,650.
TOTAL TO GRANTOR LETTER		1,650.

FORM 1041 NONTAXABLE INTEREST STATEMENT 3

DESCRIPTION	PRINCIPAL	INCOME
CHARLES SCHWAB & CO INC		34,680.
SUBTOTALS		34,680.
TOTAL TO GRANTOR LETTER		34,680.

THE 1999 ROBERT L PIERCE GRANTOR TRUST A 58-6388592

FORM 1041 FOOTNOTES STATEMENT 4

DURING THE YEAR THE PROCEEDS OF A SHORT SALE NOT CLOSED BY THE TAXPAYER IN THIS TAX YEAR WERE RECEIVED.

Transferor's Statement under
Reg 1.351-3(a)
The 1999 Robert I. Pierce Grantor Trust A FBO Julia M Pierce
EIN 88-6300052
From 1041, Tax Year Ending 12/31/1999

1. Description of property transferred.
Property transferred by The 1999 Robert I. Pierce Grantor Trust
UIA dtd. 4/21/99 Trust A FBO Julia Margaret Pierce on June 14, 1999

Property
.0531% Interest in Hesse Concrete Supply LLC EIN 56-2136357

2. Cost or basis in hands of transferor as of date of transfer
The 1999 Robert I. Pierce Grantor Trust UIA dtd 4/21/99
Trust A FBO Julia Margaret Pierce on June 14, 1999 $ 2,383,331.83

3. i. Total issued and outstanding qualified stock immediately
prior to the exchange 9,390

ii. Total issued and outstanding control stock immediately
after the exchange 9,390

iii. Stock issued in the exchange None

Shares owned by transferor immediately prior to and after
the exchange:

The 1999 Robert I. Pierce Grantor Trust UIA dtd 4/21/99
Trust A FBO Julia Margaret Pierce on June 14, 1999 2,139.8

iii. Fair market value of stock issued to transferor Not applicable

4. i. Principal amount and terms of all securities exchanged immediately
prior to and immediately after the exchange Not applicable

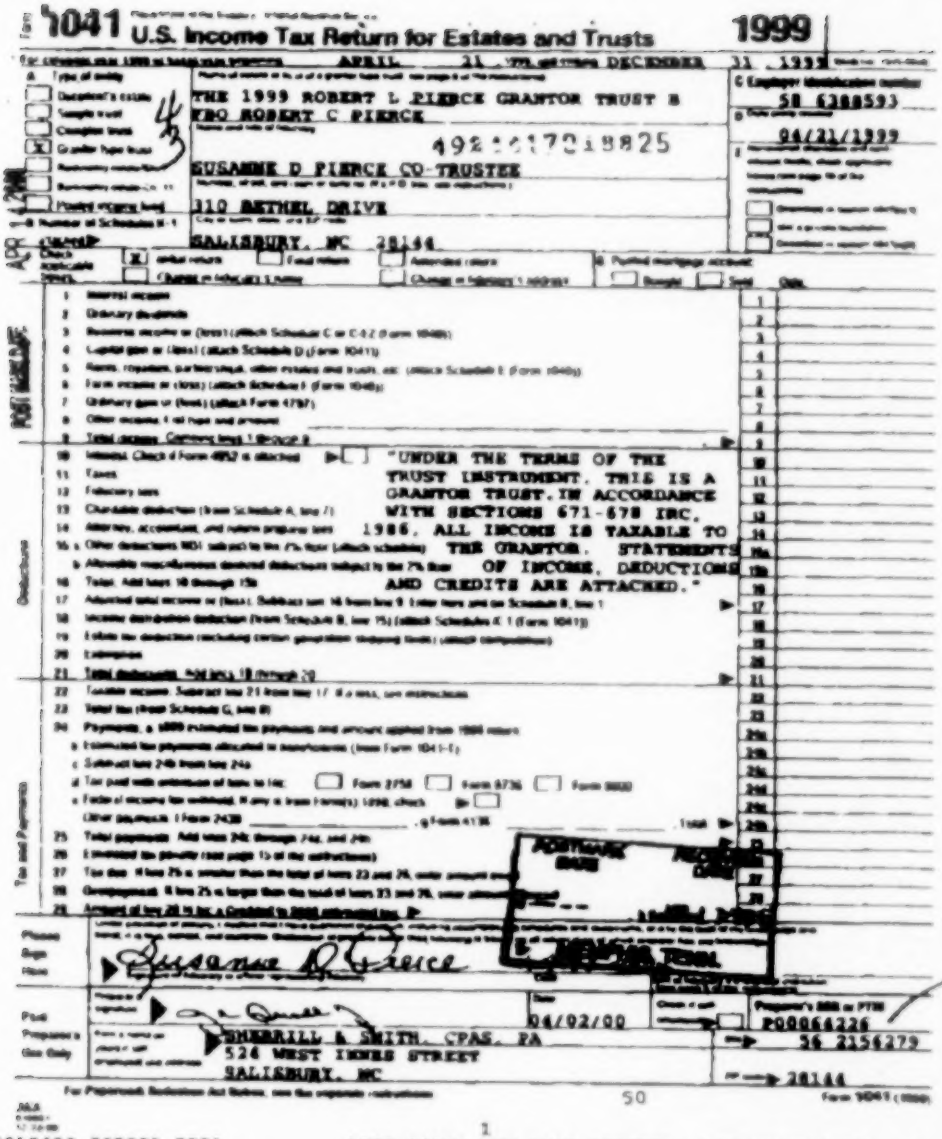
ii. Principal amount and terms of all securities issued to transferors in the
exchange and the transferor's holdings of securities immediately prior to
and immediately after the exchange Not applicable

iii. Fair market value of securities issued to transferor Not applicable

5. Amount of money exchanged to transferors None

6. Other property which was exchanged to transferors None

7. Liabilities assumed by the controlled corporation in the exchange None



Form 1041 U.S. Income Tax Return for Estates and Trusts 1999

For calendar year 1999 or fiscal year beginning APRIL 21, 1999 and ending DECEMBER 31, 1999

A Type of entity
- Decedent's estate
- Simple trust
- Complex trust
- [X] Grantor type trust
- Bankruptcy estate-Ch. 7
- Bankruptcy estate-Ch. 11
- Pooled income fund

B Number of Schedules K-1 attached

THE 1999 ROBERT L PIERCE GRANTOR TRUST B
FBO ROBERT C PIERCE

C Employer identification number: 58 6388593

D Date entity created: 04/21/1999

E Nonexempt charitable and split-interest trusts, check applicable boxes (see page 19 of the instructions)

492-60-8825

SUSANNE D PIERCE CO-TRUSTEE

310 BETHEL DRIVE

SALISBURY, NC 28144

F Check applicable boxes: [X] Initial return [ ] Final return [ ] Amended return [ ] Change in fiduciary's name [ ] Change in fiduciary's address

G Pooled mortgage account: [ ] Yes [ ] No

Income	1	Interest income	1
	2	Ordinary dividends	2
	3	Business income or (loss). Attach Schedule C or C-EZ (Form 1040)	3
	4	Capital gain or (loss). Attach Schedule D (Form 1041)	4
	5	Rents, royalties, partnerships, other estates and trusts, etc. Attach Schedule E (Form 1040)	5
	6	Farm income or (loss). Attach Schedule F (Form 1040)	6
	7	Ordinary gain or (loss). Attach Form 4797	7
	8	Other income. List type and amount	8
	9	Total income. Combine lines 1 through 8	9
Deductions	10	Interest. Check if Form 4952 is attached [ ]	10
	11	Taxes	11
	12	Fiduciary fees	12
	13	Charitable deduction (from Schedule A, line 7)	13
	14	Attorney, accountant, and return preparer fees	14
	15a	Other deductions NOT subject to the 2% limit (attach schedule)	15a
	b	Allowable miscellaneous itemized deductions subject to the 2% limit	15b
	16	Total. Add lines 10 through 15b	16
	17	Adjusted total income or (loss). Subtract line 16 from line 9. Enter here and on Schedule B, line 1	17
	18	Income distribution deduction (from Schedule B, line 15). Attach Schedules K-1 (Form 1041)	18
	19	Estate tax deduction (including certain generation-skipping taxes) (attach computation)	19
	20	Exemption	20
	21	Total deductions. Add lines 18 through 20	21
Tax and Payments	22	Taxable income. Subtract line 21 from line 17. If a loss, see instructions	22
	23	Total tax (from Schedule G, line 8)	23
	24a	Payments: a 1999 estimated tax payments and amount applied from 1998 return	24a
	b	Estimated tax payments allocated to beneficiaries (from Form 1041-T)	24b
	c	Subtract line 24b from line 24a	24c
	d	Tax paid with extension of time to file: [ ] Form 2758 [ ] Form 8736 [ ] Form 8800	24d
	e	Federal income tax withheld. If any is from Form(s) 1099, check [ ]	24e
		Other payments. List Form 2439 _____ g Form 4136 _____ Total	24g
	25	Total payments. Add lines 24c through 24e, and 24g	25
	26	Estimated tax penalty (see page 15 of the instructions)	26
	27	Tax due. If line 25 is smaller than the total of lines 23 and 26, enter amount owed	27
	28	Overpayment. If line 25 is larger than the total of lines 23 and 26, enter amount overpaid	28
	29	Amount of line 28 to be: a Credited to 2000 estimated tax [ ]	29

POSTMARK DATE

RECEIVED DATE

Please Sign Here

Signature of fiduciary or officer representing fiduciary

Date

Check if self-employed [ ]

Preparer's SSN or PTIN P00064226

Paid Preparer's Use Only

Preparer's signature

Date 04/02/00

Firm's name (or yours if self-employed) and address
SHERRILL & SMITH, CPAS, PA
524 WEST INNES STREET
SALISBURY, NC

EIN 56 2156279

ZIP code 28144

For Paperwork Reduction Act Notice, see the separate instructions

JSA

Form 1041 (1999)

50

1

09210402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 2

DOJ-018316

Form 1041 (1999) THE 1999 ROBERT L PIERCE GRANTOR TRUST B 58-6388593 Page 2

Schedule A | **Charitable Deduction.** Do not complete for a simple trust or a pooled income fund.

1	Amounts paid or permanently set aside for charitable purposes from gross income (see instructions)	1
2	Tax-exempt interest allocable to charitable contributions (see instructions)	2
3	Subtract line 2 from line 1	3
4	Capital gains for the tax year allocated to corpus and paid or permanently set aside for charitable purposes	4
5	Add lines 3 and 4	5
6	Section 1202 exclusion allocable to capital gains paid or permanently set aside for charitable purposes (see instructions)	6
7	Charitable deduction. Subtract line 6 from line 5 (enter here and on page 1, line 11)	7

Schedule B | **Income Distribution Deduction**

1	Adjusted total income (from page 1, line 17) (see instructions)	1
2	Adjusted tax-exempt interest	2
3	Total net gain from Schedule D (Form 1041), line 16, column (1) (see instructions)	3
4	Enter amount from Schedule A, line 4 (reduced by any allocable section 1202 exclusion)	4
5	Capital gains for the tax year included on Schedule A, line 1 (see instructions)	5
6	Enter any gain from page 1, line 4, as a negative number. If page 1, line 4, is a loss, enter the loss as a positive number	6
7	Distributable net income (DNI). Combine lines 1 through 6. If zero or less, enter -0-	7
8	If a complex trust, enter accounting income for the tax year as determined under the governing instrument and applicable local law	8
9	Income required to be distributed currently	9
10	Other amounts paid, credited, or otherwise required to be distributed	10
11	Total distributions. Add lines 9 and 10. If greater than line 8, see instructions.	11
12	Enter the amount of tax-exempt income included on line 11	12
13	Tentative income distribution deduction. Subtract line 12 from line 11	13
14	Tentative income distribution deduction. Subtract line 7 from line 7. If zero or less, enter -0-	14
15	Income distribution deduction. Enter the smaller of line 13 or line 14 here and on page 1, line 18	15

Schedule G | **Tax Computation**

1	Tax: a ☐ Tax rate schedule or ☐ Schedule D (Form 1041)	1a	
	b Tax on lump-sum distributions (attach Form 4972)	1b	
	c Total. Add lines 1a and 1b		1c
2a	Foreign tax credit (attach Form 1116)	2a	
	b Check: ☐ Nonconventional source fuel credit ☐ Form 8834	2b	
	c General business credit. Enter here and check which forms are attached ☐ Form 3800 or ☐ Forms (specify) ▶	2c	
	d Credit for prior year minimum tax (attach Form 8801)	2d	
3	Total credits. Add lines 2a through 2d		3
4	Subtract line 3 from line 1c		4
5	Recapture taxes. Check if from ☐ Form 4255 ☐ Form 8611		5
6	Alternative minimum tax (from Schedule I, line 39)		6
7	Household employment taxes. Attach Schedule H (Form 1040)		7
8	Total tax. Add lines 4 through 7. Enter here and on page 1, line 23		8

Other Information

		Yes	No
1	Did the estate or trust receive tax-exempt income? If "Yes," attach a computation of the allocation of expenses. Enter the amount of tax-exempt interest income and exempt-interest dividends ▶ $ 34,680.	X	
2	Did the estate or trust receive all or any part of the earnings (salary, wages, and other compensation) of any individual by reason of a contract assignment or similar arrangement?		X
3	At any time during calendar year 1999, did the estate or trust have an interest in or a signature or other authority over a bank, securities, or other financial account in a foreign country? See the instructions for exceptions and filing requirements for Form TD F 90-22.1. If "Yes," enter the name of the foreign country ▶		X
4	During the tax year, did the estate or trust receive a distribution from, or was it the grantor of, or transferor to, a foreign trust? If "Yes," the estate or trust may have to file Form 3520. See instructions		X
5	Did the estate or trust receive, or pay, any qualified residence interest on seller-provided financing? If "Yes," see page 19 for required attachment		X
6	If this is an estate or a complex trust making the section 663(b) election, check here ▶ ☐		
7	To make a section 643(g)(3) election, attach Schedule D (Form 1041), and check here ▶ ☐		
8	If the decedent's estate has been open for more than 2 years, attach an explanation for the delay in closing the estate, and check here ▶ ☐		
9	Are any present or future trust beneficiaries skip persons? See instructions		X

GRANTOR LETTER

SUSANNE D PIERCE CO-TRUSTEE
310 BETHEL DRIVE
SALISBURY, NC 28144

Tax Year Ending 12/31/99

Grantor Name & Address	Name of Trust
ROBERT L PIERCE 310 BETHEL DRIVE SALISBURY, NC 28144	THE 1999 ROBERT L PIERCE GRANTOR TRUS FBO ROBERT C PIERCE
Social Security Number [redacted]	Employer ID Number 58-6388593

THE FOLLOWING INCOME, DEDUCTIONS AND CREDITS ARE TO BE REPORTED ON THE INCOME TAX RETURNS FOR THE ABOVE NAMED GRANTOR, IF REQUIRED.

FEDERAL INFORMATION	
INCOME	
INTEREST INCOME..... (ENTER ON FORM 1040, SCHEDULE B, PART I, LINE 1)	16,487.
INTEREST FROM U.S. OBLIGATIONS NOT INCLUDED ELSEWHERE..... (ENTER ON FORM 1040, SCHEDULE B, PART I, LINE 1)	15,168.
DIVIDEND INCOME..... (ENTER ON FORM 1040, SCHEDULE B, PART II, LINE 5)	1,605.
NONPASSIVE INCOME (LOSS) FROM PARTNERSHIPS..... (ENTER ON FORM 1040, SCHEDULE E, PART II)	<1,293.>
NONPASSIVE INCOME (LOSS) FROM S CORPORATIONS..... (ENTER ON FORM 1040, SCHEDULE E, PART II)	124,297.
SHORT-TERM GAIN (LOSS) FROM PARTNR, S CORPS & FIDUCIARIES.. (ENTER ON FORM 1040, SCHEDULE D, PART I)	31,116.
LONG-TERM GAIN (LOSS) FROM PARTNR, S CORPS & FIDUCIARIES... 28% RATE GAIN (LOSS) INCLUDED IN AMOUNT ABOVE..... (ENTER ON FORM 1040, SCHEDULE D, PART II)	<44,397.> 0.
ORDINARY GAIN (LOSS)..... (ENTER ON FORM 4797, PART II)	<30,410.>
DEDUCTIONS	
CHARITABLE DEDUCTION..... (ENTER ON FORM 1040, SCHEDULE A, LINE 15)	594.
TAX PREFERENCES	
DEPRECIATION ADJUSTMENT FOR POST 1986 PROPERTY..... (ENTER ON FORM 6251, LINE 8)	2,391.
ADJUSTED GAIN OR LOSS.....	<175,080.>

DOJ-018318

GRANTOR NAME:
ROBERT L PIERCE

SOC. SEC. NUMBER:
[redacted]

(ENTER ON FORM 6251, LINE 9)

TAX-EXEMPT

MUNICIPAL TAX-EXEMPT INTEREST
(ENTER ON FORM 1040, LINE 8B)

NORTH CAROLINA TAX-EXEMPT INTEREST..... 34,680.

NORTH CAROLINA INFORMATION

SUBTRACTIONS

INTEREST ON U.S. OBLIGATIONS..... 15,168.
(ENTER ON FORM D-400, LINE 42)

CREDITS AND TAXES

OTHER CREDITS..... 246.
(ENTER ON FORM D-400TC, PART 4, LINE 25)

SCHEDULE E (Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Supplemental Income and Loss

(From rental real estate, royalties, partnerships, S corporations, estates, trusts, REMICs, etc.)

▶ Attach to Form 1040 or Form 1041. ▶ See Instructions for Schedule E (Form 1040).

OMB No. 1545-0074

1999

Attachment Sequence No. 13

Name(s) shown on return

THE 1999 ROBERT L PIERCE GRANTOR TRUST B
FBO ROBERT C PIERCE

Your social security number

58-6388593

Part I Income or Loss From Rental Real Estate and Royalties Note. Report income and expenses from your business of renting personal property on Schedule C or C-EZ. Report farm rental income or loss from Form 4835 on page 2, line 39.

1 Show the kind and location of each rental real estate property:

A
B
C

2 For each rental real estate property listed on line 1, did you or your family use it during the tax year for personal purposes for more than the greater of:
- 14 days, or
- 10% of the total days rented at fair rental value?
(See page E-1.)

	Yes	No
A		
B		
C		

Income:		Properties A	Properties B	Properties C	Totals (Add columns A, B, and C.)
3 Rents received	3				3
4 Royalties received	4				4
Expenses:					
5 Advertising	5				
6 Auto and travel (see page E-2)	6				
7 Cleaning and maintenance	7				
8 Commissions	8				
9 Insurance	9				
10 Legal and other professional fees	10				
11 Management fees	11				
12 Mortgage interest paid to banks, etc. (see page E-2)	12				12
13 Other interest	13				
14 Repairs	14				
15 Supplies	15				
16 Taxes	16				
17 Utilities	17				
18 Other (list) ▶	18				
19 Add lines 5 through 18	19				19
20 Depreciation expense or depletion (see page E-3)	20				20
21 Total expenses. Add lines 19 and 20	21				
22 Income or (loss) from rental real estate or royalty properties. Subtract line 21 from line 3 (rents) or line 4 (royalties). If the result is a (loss), see page E-3 to find out if you must file Form 6198	22				
23 Deductible rental real estate loss. Caution: Your rental real estate loss on line 22 may be limited. See page E-3 to find out if you must file Form 8582. Real estate professionals must complete line 42 on page 2	23				
24 Income. Add positive amounts shown on line 22. Do not include any losses					24
25 Losses. Add royalty losses from line 22 and rental real estate losses from line 23. Enter the total losses here					25 ( )
26 Total rental real estate and royalty income or (loss). Combine lines 24 and 25. Enter the result here. If Parts II, III, IV, and line 39 on page 2 do not apply to you, also enter this amount on Form 1040, line 17. Otherwise, include this amount in the total on line 40 on page 2					26 0.

For Paperwork Reduction Act Notice, see Form 1040 instructions. 5 Schedule E (Form 1040) 1999

09210402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 2

Schedule E (Form 1040) [illegible] Page 2

THE 1999 ROBERT L PIERCE GRANTOR TRUST B
FBO ROBERT C PIERCE

Your social security number: 58-6188593

Note: If you report amounts from farming or fishing on Schedule E, you must enter your gross income from those activities on line 41 below. Real Estate professionals must complete line 42 below.

Part II Income or Loss From Partnerships and S Corporations Note: If you report a loss from an at-risk activity, you MUST check either column (e) or (f) on line 27 to describe your investment in the activity. If you check column (f), you must attach Form 6198.

27	(a) Name	(b) Enter P for partnership; S for S corporation	(c) Check if foreign partnership	(d) Employer identification number	(e) All is not at risk	(f) Some is not at risk
A	HOME OIL & COAL INC	S		56-0546791	X	
B	HOME CONCRETE & SUPPLY, LLC	P		56-2136387	X	
C						
D						
E						

	Passive Income and Loss			Nonpassive Income and Loss	
	(g) Passive loss allowed (attach Form 8582 if required)	(h) Passive income from Schedule K-1	(i) Nonpassive loss from Schedule K-1	(j) Section 179 expense deduction from Form 4562	(k) Nonpassive income from Schedule K-1
A					124,297.
B			1,293.		
C					
D					
E					
28a	Totals				124,297.
b	Totals		1,293.		
29	Add columns (h) and (k) of line 28a				29 124,297.
30	Add columns (g), (i), and (j) of line 28b				30 (1,293.)
31	Total partnership and S corporation income or (loss). Combine lines 29 and 30. Enter the result here and include in the total on line 40 below				31 123,004.

Part III Income or Loss From Estates and Trusts

32	(a) Name	(b) Employer identification number
A		
B		

	Passive Income and Loss		Nonpassive Income and Loss	
	(c) Passive deduction or loss allowed (attach Form 8582 if required)	(d) Passive income from Schedule K-1	(e) Deduction or loss from Schedule K-1	(f) Other income from Schedule K-1
A				
B				
33a	Totals			
b	Totals			
34	Add columns (d) and (f) of line 33a			34
35	Add columns (c) and (e) of line 33b			35 ( )
36	Total estate and trust income or (loss). Combine lines 34 and 35. Enter the result here and include in the total on line 40 below			36

Part IV Income or Loss From Real Estate Mortgage Investment Conduits (REMICs) - Residual Holder

37	(a) Name	(b) Employer identification number	(c) Excess inclusion from Schedules Q, line 2c	(d) Taxable income (net loss) from Schedules Q, line 1b	(e) Income from Schedules Q, line 3b

38 Combine columns (d) and (e) only. Enter the result here and include in the total on line 40 below — 38

Part V Summary

39	Net farm rental income or (loss) from Form 4835. Also, complete line 41 below		39
40	TOTAL income or (loss). Combine lines 26, 31, 35, 38, and 39. Enter the result here and on Form 1040, line 17	▶	40 123,004.
41	Reconciliation of Farming and Fishing Income. Enter your gross farming and fishing income reported on Form 4835, line 7; Schedule K-1 (Form 1065), line 15b; Schedule K-1 (Form 1120S), line 23; and Schedule K-1 (Form 1041), line 14 (see page E-6)	41	
42	Reconciliation for Real Estate Professionals. If you were a real estate professional (see the net income or (loss) you reported anywhere on Form 1040 from all rental real estate activities in which you materially participated under the passive activity loss rules	42	

Schedule E (Form 1040) 1999

09210402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 2

DOJ-018321

1999 Income from Passthroughs

HOME OIL & COAL INC
I.D. NUMBER: 56-0546791
TYPE: S CORPORATION

ACTIVITY INFORMATION:

HOME OIL & COAL INC

TRADE OR BUSINESS - MATERIAL PARTICIPATION

ORDINARY INCOME (LOSS)	126,297
SCHEDULE E ACTIVITY INCOME (LOSS)	126,297

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	2,057
ADJUSTED GAIN OR LOSS	-174,034

OTHER K-1 INFORMATION:

INTEREST - TOTAL	16,459
SHORT-TERM CAPITAL GAIN (LOSS)	30,930
LONG-TERM CAPITAL GAIN (LOSS)	-66,131
CONTRIBUTIONS	594
SECTION 1231 GAIN (LOSS)	-30,236

DOJ-018322

1999 Income from Passthroughs

HOME CONCRETE & SUPPLY, LLC
I.D. NUMBER: 56-2136387
TYPE: PARTNERSHIP

ACTIVITY INFORMATION:

HOME CONCRETE & SUPPLY, LLC		
TRADE OR BUSINESS - MATERIAL PARTICIPATION		
ORDINARY INCOME (LOSS)	-1,293	
SCHEDULE E ACTIVITY INCOME (LOSS)		-1,293

TAX PREFERENCE ITEMS:

DEPRECIATION ADJUSTMENT FOR POST-1986 PROPERTY	334
ADJUSTED GAIN OR LOSS	-1,046

OTHER K-1 INFORMATION:

INTEREST - TOTAL	28
SHORT-TERM CAPITAL GAIN (LOSS)	186
LONG-TERM CAPITAL GAIN (LOSS)	-266
SECTION 1231 GAIN (LOSS)	-182

DOJ-018323

Form **4797** — Sales of Business Property — 1999

THE 1999 ROBERT L PIERCE GRANTOR TRUST B
FBO ROBERT C PIERCE — 58-6388593

1 Enter here the gross proceeds from the sale or exchange of real estate reported to you for 1999 on Form(s) 1099-B

Part I Sales or Exchanges of Property Used in a Trade or Business and Involuntary Conversions From Other Than Casualty or Theft - Property Held More Than 1 Year

(a) Description of property	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)	(d) Gross sales price	(e) Depreciation allowed or allowable since acquisition	(f) Cost or other basis, plus improvements and expense of sale	(g) GAIN or (LOSS) Subtract (f) from the sum of (d) and (e)
2						
HOME OIL & COAL, INC						<10,236.>
HOME CONCRETE & SUPPLY, LLC						<182.>

3	Gain, if any, from Form 4684, line 39	3
4	Section 1231 gain from installment sales from Form 6252, line 26 or 37	4
5	Section 1231 gain or (loss) from like-kind exchanges from Form 8824	5
6	Gain, if any, from line 32, from other than casualty or theft	6
7	Combine lines 2 through 6. Enter gain or (loss) here, and on the appropriate line as follows: Partnerships (except electing large partnerships). Report the gain or (loss) following the instructions for Form 1065, Schedule K, line 9. Skip lines 8, 9, 11, and 12 below. S corporations. Report the gain or (loss) following the instructions for Form 1120S, Schedule K, lines 5 and 6. Skip lines 8, 9, 11, and 12 below, unless line 7 is a gain and the S corporation is subject to the capital gains tax. All others. If line 7 is zero or a loss, enter the amount from line 7 on line 11 below and skip lines 8 and 9. If line 7 is a gain and you did not have any prior year section 1231 losses, or they were recaptured in an earlier year, enter the gain from line 7 as a long-term capital gain on Schedule D and skip lines 8, 9, and 12 below.	7	<10,418.>
8	Nonrecaptured net section 1231 losses from prior years	8	
9	Subtract line 8 from line 7. If zero or less, enter -0-. If not zero, enter on the appropriate line as follows: S corporations. Enter any gain from line 9 on Schedule D (Form 1120S), line 14, and skip lines 11 and 12 below. All others. If line 9 is zero, enter the gain from line 7 on line 12 below. If line 9 is more than zero, enter the amount from line 8 on line 12 below, and enter the gain from line 9 as a long-term capital gain on Schedule D	9	

Part II Ordinary Gains and Losses

10 Ordinary gains and losses not included on lines 11 through 17 (include property held 1 year or less):

11	Loss, if any, from line 7	11	<10,418.>
12	Gain, if any, from line 7 or amount from line 8, if applicable	12	
13	Gain, if any, from line 31	13	
14	Net gain or (loss) from Form 4684, lines 31 and 38a	14	
15	Ordinary gain from installment sales from Form 6252, line 25 or 36	15	
16	Ordinary gain or (loss) from like-kind exchanges from Form 8824	16	
17	Recapture of section 179 expense deduction for partners and S corporation shareholders from property dispositions by partnerships and S corporations	17	
18	Combine lines 10 through 17. Enter gain or (loss) here, and on the appropriate line as follows:	18	<10,418.>
a	For all except individual returns. Enter the gain or (loss) from line 18 on the return being filed.		
b	For individual returns: (1) If the loss on line 11 includes a loss from Form 4684, line 35, column (b)(ii), enter that part of the loss here. Enter the part of the loss from income-producing property on Schedule A (Form 1040), line 27, and the part of the loss from property used as an employee on Schedule A (Form 1040), line 22. Identify as from "Form 4797, line 18b(1)."	18b(1)	
	(2) Redetermine the gain or (loss) on line 18, excluding the loss, if any, on line 18b(1). Enter here and on Form 1040, line 14	18b(2)	<10,418.>

LHA For Paperwork Reduction Act Notice, see separate instructions. Form 4797 (1999)

09210402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 2

Form 4797 (1999) FBO ROBERT C PIERCE 58-6388593 Page 2

Part III Gain From Disposition of Property Under Sections 1245, 1250, 1252, 1254, and 1255

19 (a) Description of section 1245, 1250, 1252, 1254, or 1255 property:	(b) Date acquired (mo., day, yr.)	(c) Date sold (mo., day, yr.)
A		
B		
C		
D		

These columns relate to the properties on lines 19A through 19D. ▶		Property A	Property B	Property C	Property D
20 Gross sales price (Note: See line 1 before completing.)	20				
21 Cost or other basis plus expense of sale	21				
22 Depreciation (or depletion) allowed or allowable	22				
23 Adjusted basis. Subtract line 22 from line 21	23				
24 Total gain. Subtract line 23 from line 20	24				
25 If section 1245 property:					
a Depreciation allowed or allowable from line 22	25a				
b Enter the smaller of line 24 or 25a	25b				
26 If section 1250 property: If straight line depreciation was used, enter -0- on line 26g, except for a corporation subject to section 291.					
a Additional depreciation after 1975	26a				
b Applicable percentage multiplied by the smaller of line 24 or line 26a	26b				
c Subtract line 26a from line 24. If residential rental property or line 24 is not more than line 26a, skip lines 26d and 26e	26c				
d Additional depreciation after 1969 and before 1976	26d				
e Enter the smaller of line 26c or 26d	26e				
f Section 291 amount (corporations only)	26f				
g Add lines 26b, 26e, and 26f	26g				
27 If section 1252 property: Skip this section if you did not dispose of farmland or if this form is being completed for a partnership (other than an electing large partnership).					
a Soil, water, and land clearing expenses	27a				
b Line 27a multiplied by applicable percentage	27b				
c Enter the smaller of line 24 or 27b	27c				
28 If section 1254 property:					
a Intangible drilling and development costs, expenditures for development of mines and other natural deposits, and mining exploration costs	28a				
b Enter the smaller of line 24 or 28a	28b				
29 If section 1255 property:					
a Applicable percentage of payments excluded from income under section 126	29a				
b Enter the smaller of line 24 or 29a	29b				

Summary of Part III Gains. Complete property columns A through D through line 29b before going to line 30.

30 Total gains for all properties. Add property columns A through D, line 24	30	
31 Add property columns A through D, lines 25b, 26g, 27c, 28b, and 29b. Enter here and on line 13	31	
32 Subtract line 31 from line 30. Enter the portion from casualty or theft on Form 4684, line 33. Enter the portion from other than casualty or theft on Form 4797, line 6	32	

Part IV Recapture Amounts Under Sections 179 and 280F(b)(2) When Business Use Drops to 50% or Less

		(a) Section 179	(b) Section 280F(b)(2)
33 Section 179 expense deduction or depreciation allowable in prior years	33		
34 Recomputed depreciation	34		
35 Recapture amount. Subtract line 34 from line 33	35		

Form 4797 (1999)

09210402 767285 7251 1999.05200 THE 1999 ROBERT L PIERCE GR 7251 2

DOJ-018325

[illegible] PIERCE GRANTOR TRUST B 58-6388593

FORM 1041 INTEREST STATEMENT 1

DESCRIPTION	U.S. INTEREST	OTHER TAXABLE INTEREST
T ALEX BROWN INC	46,515.	
ONE OIL & COAL, INC.	<31,150.>	
ONE CONCRETE & SUPPLY LLC	<18".>	
ONE OIL & COAL INC - REGULAR INTEREST		16,859.
ONE CONCRETE & SUPPLY, LLC REGULAR INTEREST		28.
UBTOTALS	15,168.	16,887.
OTAL TO GRANTOR LETTER		31,685.

FORM 1041 DIVIDENDS STATEMENT 2

DESCRIPTION	U.S. INTEREST	REGULAR DIVIDENDS
HARLES SCHWAB & CO INC		1,494.
T ALEX BROWN		111.
UBTOTALS		1,605.
OTAL TO GRANTOR LETTER		1,605.

FORM 1041 NONTAXABLE INTEREST STATEMENT 3

DESCRIPTION	PRINCIPAL	INCOME
HARLES SCHWAB & CO INC		34,680.
UBTOTALS		34,680.
OTAL TO GRANTOR LETTER		34,680.

THE 1999 ROBERT L PIERCE GRANTOR TRUST B 58-6388593

FORM 1041 FOOTNOTES STATEMENT 4

DURING THE YEAR THE PROCEEDS OF A SHORT SALE NOT CLOSED BY THE TAXPAYER IN THIS TAX YEAR WERE RECEIVED.

Transferor's Statement under
Reg 1.351-3(b)
The 1998 Robert L Pierce Grantor Trust B FBO Robert C. Pierce
EIN: 86-6360683
From 1041, Tax Year Ending 12/31/1998

1. Description of property transferred.
Property transferred by: The 1998 Robert L Pierce Grantor Trust
U/A dtd. 4/21/98 Trust B FBO Robert Crain Pierce on June 14, 1999

Property
.0831% interest in Home Concrete Supply LLC EIN 86-2138387

2. Cost or basis in hands of transferor as of date of transfer
The 1998 Robert L Pierce Grantor Trust U/A dtd 4/21/98
Trust A FBO Robert Crain Pierce on June 14, 1999 $ 2,383,231.65

3. i. Total issued and outstanding capital stock immediately prior to the exchange 8,368

ii. Total issued and outstanding capital stock immediately after the exchange 8,368

iii. Stock issued in the exchange None

Shares owned by transferor immediately prior to and after the exchange:

The 1998 Robert L Pierce Grantor Trust U/A dtd 4/21/98
Trust A FBO Robert Crain Pierce on June 14, 1999 2,136.8

iv. Fair market value of stock issued to transferor: Not applicable

4. i. Principal amount and terms of all securities outstanding immediately prior to and immediately after the exchange Not applicable

ii. Principal amount and terms of all securities issued to transferor in the exchange and the transferor's holdings of securities immediately prior to and immediately after the exchange: Not applicable

iii. Fair market value of securities issued to transferor: Not applicable

5. Amount of money passed to transferor: None

6. Other property which was passed to transferor: None

7. Liabilities assumed by the controlled corporation in the exchange: None

DOJ-018327

PETITIONER'S BRIEF

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

BRIEF FOR THE UNITED STATES

DONALD B. VERRILLI, JR.
Solicitor General
Counsel of Record
TAMARA W. ASHFORD
Deputy Assistant Attorney General
MALCOLM L. STEWART
Deputy Solicitor General
JEFFREY B. WALL
Assistant to the Solicitor General
GILBERT S. ROTHENBERG
MICHAEL J. HAUNGS
JOAN I. OPPENHEIMER
Attorneys
Department of Justice
Washington, D.C. 20530-0001
SupremeCtBriefs@usdoj.gov
(202) 514-2217

QUESTIONS PRESENTED

As a general matter, the Internal Revenue Service (IRS) has three years to assess additional tax if the agency believes that the taxpayer's return has understated the amount of tax owed. 26 U.S.C. 6501(a). That period is extended to six years, however, if the taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the [taxpayer's] return." 26 U.S.C. 6501(e)(1)(A). The questions presented are as follows:

1. Whether an understatement of gross income attributable to an overstatement of basis in sold property is an "omi[ssion] from gross income" that can trigger the extended six-year assessment period.

2. Whether a final regulation promulgated by the Department of the Treasury, which reflects the IRS's view that an understatement of gross income attributable to an overstatement of basis can trigger the extended six-year assessment period, is entitled to judicial deference.

PARTIES TO THE PROCEEDINGS

Petitioner is the United States of America.

Respondents are Home Concrete & Supply, LLC; Robert L. Pierce; Susanne D. Pierce; Stephen R. Chandler; Rebecca R. Chandler; and Home Oil and Coal Company, Inc.

TABLE OF CONTENTS

Page

Opinions below 1
Jurisdiction 1
Statutory and regulatory provisions involved 2
Statement 2
Summary of argument 10
Argument 13
By overstating their bases in Home Concrete and thereby understating their actual gain from its sale, respondents omitted substantial amounts from their gross income, triggering the extended six-year assessment period in 26 U.S.C. 6501(e)(1)(A) 14
A. Section 6501(e)(1)(A) establishes that an overstatement of basis can trigger the six-year assessment period 14
1. The phrase "omi[ssion] from gross income" is naturally construed to encompass an understatement of taxable gain attributable to an overstatement of basis 15
2. Adjacent statutory provisions reinforce the inference that an overstatement of basis can trigger the extended six-year assessment period 20
3. The statutory purpose strongly supports extending the period for discovery of a basis overstatement 24
B. The recent Treasury regulation resolves any statutory ambiguity by specifying that an overstatement of basis triggers the six-year assessment period 27
1. The final regulation was validly promulgated ... 28
2. The final regulation applies to this case 30
3. The final regulation is entitled to deference 37

Table of Contents—Continued: Page

4. The final regulation is not impermissibly retroactive 40
C. This Court's decision in *Colony* does not control the interpretation of the current version of Section 6501(e)(1)(A) 44
1. When it amended the relevant statutory provision in 1954, Congress made clear that a basis overstatement triggers the six-year assessment period unless the taxpayer is a trade or business 44
2. The Court in *Colony* construed the pre-1954 version of the statute without addressing the post-1954 version 47
3. *Colony* does not control the interpretation of current Section 6501(e)(1)(A) 49
4. In any event, the Treasury regulation resolves the statutory ambiguity that *Colony* identified 50
Conclusion 53

TABLE OF AUTHORITIES

Cases:

American Boat Co. v. *United States*, 583 F.3d 471 (7th Cir. 2009) 6
American Liberty Oil Co. v. *Commissioner*, 1 T.C. 386 (1942) 45
Auer v. *Robbins*, 519 U.S. 452 (1997) 32
Automobile Club v. *Commissioner*, 353 U.S. 180 (1957) 42

Cases—Continued: Page

Babbitt v. *Sweet Home Chapter of Cmtys. for a Great Or.*, 515 U.S. 687 (1995) 23

Bakersfield Energy Partners, LP v. *Commissioner*, 568 F.3d 767 (9th Cir. 2009) 22

Beard v. *Commissioner*, 633 F.3d 616 (7th Cir. 2011), petition for cert. pending, No. 10-1553 (filed June 23, 2011) 3, 4, 5, 19, 21

Bob Jones Univ. v. *United States*, 461 U.S. 574 (1983) ... 38

Bowen v. *Georgetown Univ. Hosp.*, 488 U.S. 204 (1988) 42

Brandon Ridge Partners v. *United States*, No. 8:06-cv-1340, 2007 WL 2209129 (M.D. Fla. July 30, 2007) 23

Burks v. *United States*, 633 F.3d 347 (5th Cir. 2011), petition for cert. denied, No. 11-178 (filed Aug. 11, 2011) 32, 39

CC & F W. Operations Ltd. P'ship v. *Commissioner*, 273 F.3d 402 (1st Cir. 2001) 41

Cemco Investors, LLC v. *United States*, 515 F.3d 749 (7th Cir.), cert. denied, 555 U.S. 823 (2008) 4, 6

Chevron U.S.A. Inc. v. *NRDC*, 467 U.S. 837 (1984) 12, 37, 38

Colony, Inc. v. *Commissioner*:

357 U.S. 28 (1958) ..... *passim*

26 T.C. 30 (1956), aff'd, 244 F.2d 75 (6th Cir. 1957), rev'd, 357 U.S. 28 (1958) 52

Commissioner v. *Banks*, 543 U.S. 426 (2005) 15

Commissioner v. *Glenshaw Glass Co.*, 348 U.S. 426 (1955) 16

Cases—Continued: Page

Commissioner v. *Schleier*, 515 U.S. 323 (1995) 15
Davis v. *Hightower*, 230 F.2d 549 (5th Cir. 1956) 53
Deakman-Wells Co. v. *Commissioner*, 213 F.2d 894 (3d Cir. 1954) 53
Dolan v. *USPS*, 546 U.S. 481 (2006) 24
Epsolon Ltd. v. *United States*, 78 Fed. Cl. 738 (2007) ... 33
Goodenow v. *Commissioner*, 238 F.2d 20 (8th Cir. 1956) 53
Grapevine Imports, Ltd. v. *United States*, 636 F.3d 1368 (Fed. Cir. 2011), petition for cert. pending, No. 11-163 (filed Aug. 5, 2011) 32, 39, 43
Green v. *Commissioner*, 7 T.C. 263 (1946), aff'd, 168 F.2d 994 (6th Cir. 1948) 16
Intermountain Ins. Serv. of Vail, LLC v. *Commissioner*:
650 F.3d 691 (D.C. Cir. 2011) ..... *passim*
134 T.C. 211 (2010), rev'd, 650 F.3d 691 (D.C. Cir. 2011) 35
Kennedy v. *Plan Adm'r for DuPont Sav. & Inv. Plan*, 555 U.S. 285 (2009) 32
Kornman & Assocs., Inc. v. *United States*, 527 F.3d 443 (5th Cir. 2008) 4, 5
Landgraf v. *USI Film Prods.*, 511 U.S. 244 (1994) 42
Levy v. *Sterling Holding Co.*, 544 F.3d 493 (3d Cir. 2008), cert. denied, 129 S.Ct. 2827 (2009) 40
Lindh v. *Murphy*, 521 U.S. 320 (1997) 42
Manhattan Gen. Equip. Co. v. *Commissioner*, 297 U.S. 129 (1936) 41

Cases—Continued: Page

Mayo Found. for Med. Educ. & Research v. *United States*, 131 S. Ct. 704 (2011) 37, 38, 40, 50
National Cable & Telecomms. Ass'n v. *Brand X Internet Servs.*, 545 U.S. 967 (2005) 13, 37, 50
Pliva, Inc. v. *Mensing*, 131 S. Ct. 2567 (2011) 32
Pope v. *Shalala*, 998 F.2d 473 (7th Cir. 1993), overruled on other grounds by *Johnson* v. *Apfel*, 189 F.3d 561 (7th Cir. 1999) 41
Randell v. *United States*, 64 F.3d 101 (2d Cir. 1995), cert. denied, 519 U.S. 815 (1996) 8
Reis v. *Commissioner*, 142 F.2d 900 (6th Cir. 1944) 45
Rhone-Poulenc Surfactants & Specialties, L.P. v. *Commissioner*, 114 T.C. 533 (2000), appeal dismissed, 249 F.3d 175 (3d Cir. 2001) 33
Robinson v. *Shell Oil Co.*, 519 U.S. 337 (1997) 35
Salman Ranch Ltd v. *United States*, 573 F.3d 1362 (Fed. Cir. 2009) 22
Salman Ranch Ltd. v. *United States*, 647 F.3d 929 (10th Cir. 2011), petition for cert. pending, No. 11-582 (filed Nov. 7, 2011) 32, 39, 43
Slaff v. *Commissioner*, 220 F.2d 65 (9th Cir. 1955) 53
Smiley v. *Citibank (S.D.), N.A.*, 517 U.S. 735 (1996) 40, 41
Stobie Creek Invs., LLC v. *United States*, 608 F.3d 1366 (Fed. Cir. 2010) 4
UTAM, Ltd. v. *Commissioner*, 645 F.3d 415 (D.C. Cir. 2011) 33
United States v. *Heirs of Boisdoré*, 49 U.S. (8 How.) 113 (1849) 24

Cases—Continued: Page

United States v. *Morton*, 467 U.S. 822 (1984) 40, 50
United States v. *Tinklenberg*, 131 S. Ct. 2007 (2011) 49
Uptegrove Lumber Co. v. *Commissioner*, 204 F.2d 570 (3d Cir. 1953) 45, 53

Statutes and regulations:

Administrative Procedure Act, 5 U.S.C. 553 29
Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, § 513, 124 Stat. 111 2
Internal Revenue Code (26 U.S.C.):
Section 61 16
Section 61(a) 15, 16
Section 61(a)(3) 2, 10, 16
Section 701 8
Sections 701-704 8
Section 708(b)(1)(B) 7
Section 722 4
Section 723 4
Section 743(b)(1) 7
Section 752 ..... 4, 6
Section 754 7
Section 1011(a) 3
Section 1012 3
Section 6031 8
Section 6223(a) 33
Section 6229(d) 33
Section 6230(g) 31

Statutes and regulations—Continued: Page

Section 6501 2
Section 6501(a) 2, 8, 9, 27
Section 6501(e) 10, 20
Section 6501(e)(1)(A) ..... *passim*
Section 6501(e)(1)(A)(i) ..... *passim*
Section 6501(e)(1)(A)(ii) 20, 21, 24, 26, 46
Section 6501(e)(2) 11, 23, 49
Section 7121 31
Section 7481(a) 31
Section 7609(e)(2) 9
Section 7805(a) 38
Section 7805(b) 43
Section 7805(b)(8) 42
Section 7805(e)(1) 29
Internal Revenue Code of 1939:
26 U.S.C. 275(c) (1940) ..... *passim*
26 U.S.C. 3791(b) (1940) 42
Revenue Act of 1934, ch. 277, § 275(c), 48 Stat. 745 (26 U.S.C. 275(c) (1934)) 44, 45
Temp. Treas. Reg. (26 C.F.R.):
Section 301.6501(e)-1T (2009) 28
Section 301.6501(e)-1T(a)(1)(iii) (2009) 28
Treas. Reg. (26 C.F.R.):
Section 1.61-6(a) 16
Section 301.6501(e)-1 27
Section 301.6501(e)-1(a)(1)(iii) 29
Section 301.6501(e)-1(e) 30

Regulations—Continued: Page

Section 301.6501(e)-1(e)(1) 29, 34
Section 301.7701-3(b)(1)(i) 6

Miscellaneous:

Bernard J. Audet, Jr., Note, *One Case To Rule Them All: The Ninth Circuit in* Bakersfield *Applies* Colony *To Deny the IRS an Extended Statute of Limitations in Overstatement of Basis Cases*, 55 Vill. L. Rev. 409 (2010) 17

Black's Law Dictionary (9th ed. 2009) 19

74 Fed. Reg. 49,354 (Sept. 28, 2009) 28

H.R. Rep. No. 1337, 83d Cong., 2d Sess. (1954) 46

I.R.S. Notice 2000-44, 2000-2 C.B. 255 4

Martha Neil, *Ex-Jenkens & Gilchrist Partners Paul Daugerdas and Donna Guerin Found Guilty in Tax Shelter Case*, A.B.A. J. Law News Now, May 24, 2011, http://www.abajournal.com/news/article/former_jenkens_gilchrist_partners_paul_daugerdas_and_donna_guerin 6

S. Rep. No. 1622, 83d Cong., 2d Sess. (1954) 46

Staff of the Joint Comm. on Internal Revenue Taxation, 84th Cong., *Summary of the New Provisions of the Internal Revenue Code of 1954* (Comm. Print 1955) 23

T.D. 9466, 2009-43 I.R.B. 531 28

T.D. 9511, 2011-6 I.R.B. 455 28

The American Heritage Dictionary of the English Language (4th ed. 2006) 18

Miscellaneous—Continued: Page

The New Shorter Oxford English Dictionary on Historical Principles (4th ed. 1993) 19
Webster's New International Dictionary of the English Language (2d ed. 1958) 18
Webster's Third New International Dictionary of the English Language (1993) 18

In the Supreme Court of the United States

No. 11-139

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-21a) is reported at 634 F.3d 249. The opinion of the district court (Pet. App. 23a-46a) is reported at 599 F. Supp. 2d 678.

JURISDICTION

The judgment of the court of appeals was entered on February 7, 2011. A petition for rehearing was denied on April 5, 2011 (Pet. App. 22a). On June 22, 2011, the Chief Justice extended the time within which to file a petition for a writ of certiorari to and including August 3, 2011, and the petition was filed on that date. The petition for a writ of certiorari was granted on September

27, 2011. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

The relevant statutory and regulatory provisions are reproduced in the appendix to the petition for a writ of certiorari. See Pet. App. 47a-72a.

STATEMENT

1. As a general matter, the Internal Revenue Service (IRS) has three years to assess additional tax if the agency believes that the taxpayer's return has understated the amount of tax owed. 26 U.S.C. 6501(a). That period is extended to six years, however, if the taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the [taxpayer's] return." 26 U.S.C. 6501(e)(1)(A). The question presented in this case is whether that six-year assessment period applies to a tax-avoidance scheme that operated by overstating a taxpayer's basis in property.[1]

a. When a taxpayer sells property, any "[g]ain[]" that he realizes from the sale contributes to his "gross income." 26 U.S.C. 61(a)(3). The taxpayer's gain, however, is not the sale price of his property. Rather, it is

---

[1] References in this brief to Section 6501 are to that section as it appears in the 2006 edition of the United States Code. There were no amendments to the pertinent provisions of Section 6501 between 1999 (which is the tax year at issue here) and 2009. In 2010, Congress amended Section 6501. See Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, § 513, 124 Stat. 111. Those amendments redesignated a portion of Section 6501(e)(1)(A) but did not alter the text in any way material to the disposition of this case.

the sale price minus the taxpayer's capital stake in the sold asset, which is generally the amount paid to obtain the property, as adjusted by various other factors. 26 U.S.C. 1012. For tax purposes, that capital stake is commonly referred to as the taxpayer's "basis" in property. 26 U.S.C. 1011(a). Because the taxable income from a property sale is generally determined by subtracting the taxpayer's basis from the property's sale price, an overstatement of basis will typically decrease the amount of the taxpayer's gain (and thus the amount of federal income-tax liability) that is attributable to the sale.

This case involves a particular kind of tax avoidance scheme, known as a Son-of-BOSS (Bond and Option Sales Strategy) transaction. In a Son-of-BOSS transaction, a taxpayer uses some mechanism, often a short sale, to artificially increase his basis in an asset before the asset is sold. A short sale is a sale of a security that the seller does not own or has not contracted for at the time of the sale. To close the short sale, the seller is obligated to purchase and deliver the security at some point in the future, often by using the proceeds from the short sale itself. Pet. App. 2a n.1. Typically in a Son-of-BOSS transaction, a taxpayer enters into a short sale and transfers the proceeds of the sale as a capital contribution to a partnership. The partnership then closes the short sale by purchasing and delivering the relevant security on the open market. See *Beard* v. *Commissioner*, 633 F.3d 616, 617-618 (7th Cir. 2011), petition for cert. pending, No. 10-1553 (filed June 23, 2011).

When the taxpayer and partnership file their tax returns for the year in which a transaction of the kind described above occurs, they are required under

26 U.S.C. 722, 723, and 752 to report their taxable bases in the partnership. The taxpayer's basis in the partnership is called an "outside basis," while the partnership's basis in its own assets is called an "inside basis." See *Kornman & Assocs., Inc.* v. *United States*, 527 F.3d 443, 456 n.12 (5th Cir. 2008). In a Son-of-BOSS transaction, when computing both "outside" and "inside" basis, the taxpayer and the partnership include the short-sale proceeds contributed as capital to the partnership, without decreasing that amount by the corresponding obligation (*i.e.*, to close the short sale by purchasing and delivering the relevant security) that the partnership has assumed. As a result of that asymmetric treatment, the taxpayer either generates a large paper loss that can be used to offset capital gains on other unrelated investments, or turns what would otherwise have been a sizeable capital gain into a smaller taxable gain or even a capital loss. See *Beard*, 633 F.3d at 618.

b. In 2000, the IRS issued a notice informing taxpayers that Son-of-BOSS transactions were invalid under the tax laws. See I.R.S. Notice 2000-44, 2000-2 C.B. 255 (describing arrangements that unlawfully "purport to give taxpayers artificially high basis in partnership interests"). Consistent with that notice, the courts of appeals have uniformly invalidated Son-of-BOSS transactions as lacking in economic substance. See, *e.g.*, *Cemco Investors, LLC* v. *United States*, 515 F.3d 749, 751 (7th Cir.) (Easterbrook, C.J.) (explaining that by accounting for the taxpayer's transfer of an asset but not a corresponding liability, a Son-of-BOSS transaction does "not accurately reflect[] * * * the deal's nature" and "seems to lack economic substance"), cert. denied, 555 U.S. 823 (2008); see also *Stobie Creek Invs., LLC* v.

United States, 608 F.3d 1366, 1376 (Fed. Cir. 2010) ("Measured either by their economic reality or their purported business purpose, the [Son-of-BOSS tax shelters] were properly disregarded under the economic substance doctrine."); cf. *Kornman & Assocs., Inc.*, 527 F.3d at 456 ("The Appellants' premeditated attempt to transform this wash transaction (for economic purposes) into a windfall (for tax purposes) is reminiscent of an alchemist's attempt to transmute lead into gold.").

In 2004, the IRS offered a settlement to approximately 1200 taxpayers. Many taxpayers who had engaged in Son-of-BOSS transactions, however, either did not qualify, chose not to participate in the settlement, or had not yet been identified. See *Beard*, 633 F.3d at 618. With respect to many of the taxpayers who did not participate in the settlement, it was critically important whether the IRS had three or six years from the filing of their returns to assess additional income taxes, because their treatment of the two parts of a Son-of-BOSS shelter (*i.e.*, the opening and closing of a short sale) as separate transactions on their tax returns made it extremely difficult for the IRS to discern that the taxpayers were in fact executing the Son-of-BOSS avoidance scheme. See J.A. 109 ("Nothing on the face of the returns connects these two disclosures together in a way that indicates that they were, in fact, the opening and closing of the same short sale transaction."); J.A. 110 ("[E]ven an IRS examiner trained in the art of divination would have been hard pressed to discern [respondents'] true actions.").

2. In this case, respondents Stephen R. Chandler and Robert L. Pierce were the sole shareholders of respondent Home Oil and Coal Company, Inc. (Home Oil),

which they planned to sell. Anticipating a substantial capital gain on the sale, they sought advice from various firms, including the law firm of Jenkens & Gilchrist, P.C., on how to minimize their tax liability. Pet. App. 2a; J.A. 41-81 (opinion letter).[2] Based on that advice, in April 1999, they formed respondent Home Concrete & Supply, LLC (Home Concrete), which was a pass-through entity designed solely for the purpose of executing the Son-of-BOSS shelter.[3] Home Concrete's five partners were Chandler, Pierce, and two trusts established for the benefit of Pierce's children (collectively, the taxpayers), as well as Home Oil. Pet. App. 2a.

On May 13, 1999, the taxpayers participated in short sales of United States Treasury Notes, receiving total cash proceeds of more than $7.4 million. On May 18, 1999, they transferred that entire amount, along with the obligation to close out the short positions, to Home Concrete. The following day, Home Concrete closed the

---

[2] Jenkens & Gilchrist, P.C., marketed thousands of similar Son-of-BOSS tax shelters to wealthy individuals for tax-avoidance purposes. The firm ultimately disbanded after agreeing to a class-action settlement of $75 million, and two of its tax partners were recently convicted on a total of 35 counts of conspiracy, tax evasion, and mail fraud. See *American Boat Co.* v. *United States*, 583 F.3d 471, 477 (7th Cir. 2009); *Cemco Investors, LLC*, 515 F.3d at 750; see also Martha Neil, *Ex-Jenkens & Gilchrist Partners Paul Daugerdas and Donna Guerin Found Guilty in Tax Shelter Case*, ABA J. Law News Now, May 24, 2011, http://www.abajournal.com/news/article/former_jenkens_gilchrist_partners_paul_daugerdas_and_donna_guerin/.

[3] Home Concrete was a limited liability corporation, which for present tax purposes is treated in the same manner as a partnership. See 26 U.S.C. 752; Treas. Reg. 301.7701-3(b)(1)(i). This brief therefore refers to the ownership interests in Home Concrete as partnership interests.

short sales by purchasing and delivering Treasury Notes for slightly less than $7.4 million. In calculating their outside bases in Home Concrete, the taxpayers included the amount of the short-sale proceeds (more than $7.4 million) that had been contributed to the company, without reducing that amount to reflect Home Concrete's offsetting obligation to close the short positions. Pet. App. 3a-4a.

In June 1999, the taxpayers executed a series of transactions through which they transferred virtually all of Home Oil's assets to Home Concrete. They also transferred percentages of their respective partnership interests in Home Concrete to Home Oil. Pet. App. 3a. Those transfers triggered the termination of the existing Home Concrete partnership and the formation of a new partnership. See 26 U.S.C. 708(b)(1)(B). The formation of that new partnership, in turn, permitted Home Concrete to adjust, or "step up," its inside basis to equal the taxpayers' outside bases. See Pet. App. 3a-4a; see also 26 U.S.C. 743(b)(1), 754. Because the taxpayers had inflated their outside bases (by including the short-sale proceeds contributed to Home Concrete, without decreasing that amount by the offsetting obligation to close the short sales), Home Concrete's new inside basis was similarly inflated. In August 1999, the taxpayers sold Home Concrete for approximately $10.6 million. Pet. App. 2a-3a.

In April 2000, Chandler and his wife, respondent Rebecca R. Chandler; Pierce and his wife, respondent Susanne D. Pierce; the two Pierce trusts; and Home Concrete filed their federal income-tax returns for 1999. Home Concrete's inflated new inside basis enabled it to report only a modest gain of $69,125 on the $10.6 million

sale of its assets. And because Home Concrete's partners were required to report their respective shares of any gain, the taxpayers reported income amounts from the asset sale that were dramatically lower than they would have been if the Son-of-BOSS transactions had not been utilized. Pet. App. 3a-4a.[4]

3. In September 2006, the IRS issued a Final Partnership Administrative Adjustment (FPAA). See Pet. App. 4a-5a; J.A. 82-97. In the FPAA, the IRS determined that Home Concrete was a sham company formed solely for tax-avoidance purposes, and it decreased to zero the taxpayers' outside bases in Home Concrete. See J.A. 95-96. If this Court holds that the FPAA was timely, and if the substantive determinations contained in the FPAA are ultimately upheld, those determinations will have the effect of increasing Chandler and Pierce's taxable income for 1999 by approximately $6 million.

Respondents challenged the FPAA, arguing that it was issued after the expiration of the three-year assessment period provided by 26 U.S.C. 6501(a). The IRS contended that the assessments were governed instead by the extended six-year assessment period in 26 U.S.C. 6501(e)(1)(A), which applies when a taxpayer "omits from gross income an amount properly includible there-

---

[4] Partnerships do not pay federal income tax, but they are required to file annual information returns reporting the partners' distributive shares of income, gain, deductions, or credits. See 26 U.S.C. 701, 6031; *Randell* v. *United States*, 64 F.3d 101, 103 (2d Cir. 1995), cert. denied, 519 U.S. 815 (1996). The individual partners also report their respective distributive shares on their federal income tax returns. See 26 U.S.C. 701-704. Unpaid taxes are assessed against the individual partners.

in which is in excess of 25 percent of the amount of gross income stated in the return." Pet. App. 5a-6a.[5]

The district court granted partial summary judgment to the IRS. Pet. App. 23a-46a. The court ruled that "where a taxpayer overstates basis and, as a result, leaves an amount out of gross income, the taxpayer 'omits from gross income an amount properly includible therein' for purposes of [Section] 6501(e)(1)(A)." *Id.* at 39a. The court therefore concluded that the six-year period in Section 6501(e)(1)(A), rather than the three-year period in Section 6501(a), applied to the IRS's assessment. *Ibid.* The court rejected respondents' argument that this Court's decision in *Colony, Inc.* v. *Commissioner*, 357 U.S. 28 (1958) (*Colony*), required a different result. The district court explained that *Colony* had involved a predecessor version of the Internal Revenue Code, and that subsequent statutory amendments make clear that *Colony*'s holding does not apply to the current Section 6501(e)(1)(A). Pet. App. 32a-38a.

4. a. The court of appeals reversed. Pet. App. 1a-21a. The court concluded that "*Colony* forecloses the argument that Home Concrete's overstated basis in its reporting of the short sale proceeds resulted in an omission from its reported gross income." *Id.* at 11a. The court declined to apply a regulation promulgated in tem-

---

[5] Although the FPAA was issued in September 2006, more than six years after the taxpayers filed their returns in April 2000, the assessment period was suspended for approximately five months (between December 2003 and May 2004) due to Jenkens & Gilchrist, P.C.'s tardy compliance with an IRS summons. See C.A. App. 326 n.5; see also 26 U.S.C. 7609(e)(2). Respondents do not dispute that if the six-year assessment period applies, the FPAA in this case was timely.

porary form by the IRS in September 2009, which became final while the appeal in this case was pending, and which construes the phrase "omits from gross income" to encompass situations in which a taxpayer understates his income by overstating his basis in property. *Id.* at 16a. The court held that the regulation was inapplicable by its terms, and that this Court in *Colony* had found the relevant statutory language unambiguous and thus precluded any contrary agency interpretation. *Id.* at 12a-16a.

b. Judge Wilkinson concurred to express his agreement with the panel's understanding of *Colony*. Pet. App. 17a-21a.

SUMMARY OF ARGUMENT

A. The text, structure, and purpose of 26 U.S.C. 6501(e)(1)(A) establish that respondents "omit[ted] from gross income an amount properly includible therein" when they understated their gains from the sale of Home Concrete. The Internal Revenue Code defines the term "gross income" to include "[g]ains derived from dealings in property," 26 U.S.C. 61(a)(3), and respondents' "gains" from the sale of Home Concrete are calculated by subtracting their bases in the company from their shares of the sale price. By representing their bases in Home Concrete to be much larger than they actually were, respondents "omitted" from their returns substantial "amounts" of "gain," and thus of "gross income."

Two adjacent provisions within Section 6501(e) reinforce the conclusion that the six-year assessment period applies to substantial understatements of gross income that are attributable to overstatements of basis. Sub-

paragraph (i) of Section 6501(e)(1)(A) states that, "[i]n the case of a trade or business," the "gross income" a taxpayer derives from the sale of property is the total sale price, without any offset for the taxpayer's cost of acquiring the property. Subparagraph (i) eliminates the possibility that a trade or business could trigger the six-year assessment period by overstating its basis in sold property, and the provision would be largely superfluous if the phrase "omits from gross income an amount properly includible therein" *already* excluded understatements of income attributable to overstatements of basis. In addition, Section 6501(e)(2) gives the IRS six years from the filing of an estate- or gift-tax return to assess additional tax "if the taxpayer omits items includible in the gross estate." Congress referred in that provision to the omission of "items" in order to make clear that the six-year assessment period established by Section 6501(e)(2) is not triggered by undervaluation of items that are reported on the return. By contrast, Section 6501(e)(1)(A)'s use of the term "amount" rather than "item" reinforces the conclusion that the provision applies when a taxpayer acknowledges receipt of a particular item of gross income (here, gains from the sale of Home Concrete) but represents the amount of the gain to be much smaller than it actually is.

Cases like this one directly implicate the purpose of Section 6501(e)(1)(A)'s extended assessment period. The evident rationale for extending the assessment period in cases involving substantial omissions from gross income is that such omissions are often difficult to detect. A basis overstatement will typically be as difficult to detect as an understatement of sale price, and the taxpayers in this case engaged in extensive manipula-

tions to obscure their overstatements of their bases in Home Concrete.

B. To the extent the statutory language is ambiguous, the Treasury Department recently promulgated a final regulation that reasonably resolves that ambiguity. The final rule was validly adopted after notice-and-comment procedures. As the preamble to the final rule makes clear, the regulation applies to cases, like this one, in which challenges to the timeliness of Final Partnership Administrative Adjustments were pending in court on the rule's September 24, 2009, effective date. This Court recently confirmed that the principles of deference to agency authority announced in *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837 (1984), apply with full force to Treasury Department regulations that clarify ambiguous provisions of the Internal Revenue Code, and all the courts of appeals to reach *Chevron*'s second step have agreed that the final rule reflects a reasonable interpretation of the statutory language.

Contrary to respondents' contention, the regulation is not impermissibly retroactive. The rule clarified rather than changed existing law, and it addressed the procedures for assessing tax rather than the legality of respondents' primary conduct. In any event, the rule would be valid even if it had retroactive effect, because the Treasury Department has express statutory authority to promulgate retroactive rules in this context.

C. The Court's decision in *Colony, Inc.* v. *Commissioner*, 357 U.S. 28 (1958), does not control this case. In *Colony*, the Court construed a predecessor statute (26 U.S.C. 275(c) (1940)) that contained the language "omits from gross income an amount properly includible therein." Although the Court held that former Section

275(c) did not encompass understatements of gross income attributable to overstatements of basis, it recognized that the provision was ambiguous.

Because the language quoted above is ambiguous in isolation, its meaning (and, in particular, its application to understatements of gross income attributable to overstatements of basis) may vary depending on the broader statutory context. When it amended and recodified former Section 275(c) in 1954, Congress provided that the gross income of a trade or business would be calculated differently from the gross income of other taxpayers. The purpose and principal effect of that special computation method was to make clear that an overstatement of basis by a trade or business could not trigger the extended six-year assessment period. That amendment to the statutory scheme, which is limited by its terms to cases involving trades or businesses, belies any contention that Congress intended the same rule to apply to all taxpayers.

The *Colony* Court's recognition that the relevant language ("omits from gross income an amount properly includible therein") is ambiguous also means that the Treasury Department could by regulation adopt a different reasonable interpretation of the disputed text. See *National Cable & Telecomms. Ass'n* v. *Brand X Internet Servs.*, 545 U.S. 967, 982-983 (2005) (*Brand X*). Under *Brand X*, the Department could have taken that step even if the current statutory scheme were identical to the scheme at issue in *Colony*. The agency's authority to act as it did is particularly clear, however, because the Department, in construing the language quoted above, could consider the implications of later-enacted, adja-

cent statutory provisions that the *Colony* Court had no occasion to address.

ARGUMENT

BY OVERSTATING THEIR BASES IN HOME CONCRETE AND THEREBY UNDERSTATING THEIR ACTUAL GAIN FROM ITS SALE, RESPONDENTS OMITTED SUBSTANTIAL AMOUNTS FROM THEIR GROSS INCOME, TRIGGERING THE EXTENDED SIX-YEAR ASSESSMENT PERIOD IN 26 U.S.C. 6501(e)(1)(A)

An understatement of gross income attributable to an overstatement of basis in sold property is an "omi[ssion] from gross income" that can trigger the six-year assessment period in 26 U.S.C. 6501(e)(1)(A). That is the most natural reading of the disputed language, particularly when Section 6501(e)(1)(A) is read in its larger statutory context. And to the extent the statutory text is ambiguous, the Department of the Treasury has promulgated a regulation that resolves the question presented here. This Court's decision in *Colony, Inc.* v. *Commissioner*, 357 U.S. 28 (1958), does not require a different result. The Court in *Colony* addressed a predecessor statute rather than Section 6501(e)(1)(A) in its current form, and subsequent statutory amendments make clear that *Colony*'s holding does not apply to the current Section 6501(e)(1)(A).

A. Section 6501(e)(1)(A) Establishes That An Overstatement Of Basis Can Trigger The Six-Year Assessment Period

The statutory text, structure, and purpose establish that respondents' understatement of their gain from the sale of Home Concrete was an "omi[ssion] from gross

income [of] an amount properly includible therein" that triggered the six-year assessment period in 26 U.S.C. 6501(e)(1)(A). That is so even though respondents' understatement of gain was attributable to an overstatement of basis in their partnership interests, rather than (for example) to an understatement of the sale proceeds.

1. The phrase "omi[ssion] from gross income" is naturally construed to encompass an understatement of taxable gain attributable to an overstatement of basis

Under Section 6501(e)(1)(A), the IRS has six years from the filing of a return to assess additional taxes "[i]f the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return." Respondents do not dispute that the amount of income at issue here—approximately $6 million—is "in excess of 25 percent of the amount of gross income stated in the return." 26 U.S.C. 6501(e)(1)(A). The question is whether the taxpayers "omit[ted]" that "amount" from their "gross income" when they (i) overstated their bases in Home Concrete, (ii) subtracted those inflated amounts from their shares of the sale proceeds, and (iii) thereby reported on their tax returns gains from the sale of Home Concrete that were a tiny fraction of their actual gains.

a. Section 61(a) of the Internal Revenue Code "defines 'gross income' for federal tax purposes as 'all income from whatever source derived.'" *Commissioner* v. *Banks*, 543 U.S. 426, 433 (2005). That definition "extends broadly to all economic gains not otherwise exempted." *Ibid.*; see *Commissioner* v. *Schleier*, 515 U.S. 323, 327 (1995) ("We have repeatedly emphasized the

'sweeping scope' of this section and its statutory predecessors.") (quoting *Commissioner* v. *Glenshaw Glass Co.*, 348 U.S. 426, 429 (1955)); *Green* v. *Commissioner*, 7 T.C. 263, 277 (1946) ("'Gross income' has a well established meaning in the revenue laws, denoting statutory gross income as defined by [the predecessor statute to Section 61]."), aff'd, 168 F.2d 994 (6th Cir. 1948). Section 61(a) thus requires a taxpayer to treat as "gross income" any income received from any source, unless that income is specifically excepted by another provision of the Internal Revenue Code.

Of particular relevance here, the term "gross income" as defined in Section 61(a) encompasses "[g]ains derived from dealings in property." 26 U.S.C. 61(a)(3); see Treas. Reg. 1.61-6(a) ("Gain realized on the sale or exchange of property is included in gross income, unless excluded by law."). A "gain" from a sale of property is defined, in turn, as "the excess of the amount realized over the unrecovered cost or other basis for the property sold or exchanged." *Ibid.* Because a gain on a sale of property is determined by subtracting the taxpayer's basis (or capital stake in the property) from the sale price, a taxpayer can fail to report income from a property sale either by overstating his basis in the property or by understating the property's sale price.

b. In this case, respondents concealed nearly $6 million in gross income from the IRS through a scheme that consisted of three basic steps. First, the taxpayers (Chandler, Pierce, and the two Pierce trusts) transferred $7.4 million in short-sale proceeds as capital contributions to Home Concrete. In calculating their bases in the partnership, the taxpayers did not reduce those amounts to reflect the corresponding obligation that Home Concrete simultaneously assumed to close

the short positions. Moreover, they concealed the true nature of the transactions on their returns for the 1999 tax year. Chandler and Pierce stated only that "the proceeds of a short sale not closed by the taxpayer during this tax year were received." J.A. 204, 258, 286, 299. As the district court observed, "[i]mplicit in this 'disclosure' is that Pierce and Chandler retained the short sale position and the obligation to close that short sale, which was actually not the case." J.A. 109. Nothing on the taxpayers' returns suggested either that the taxpayers had transferred both an asset and an offsetting obligation to Home Concrete or that they had treated the asset and obligation differently in order to inflate their bases in the partnership.

Second, in its return for the 1999 tax year, Home Concrete reported a transaction in United States Treasury Bonds. See J.A. 128. But Home Concrete did not indicate that the transaction was a set of short sales, let alone that the taxpayers had opened the sales and contributed the proceeds to Home Concrete, which then had closed the short positions. To the contrary, Home Concrete's return conveyed the impression that the company had purchased the bonds on May 18, 1999, for $7.36 million, sold them the next day for $7.47 million, and made a profit of approximately $113,000 in the process. *Ibid.* As the district court observed, "[t]he description of the sale itself is completely misleading" because it indicates "a straight sale of Treasury Bonds instead of the back-end of a short sale transaction." J.A. 108-109; see J.A. 109 ("[T]he only reasonable conclusion a reviewer was likely to draw was that Home Concrete engaged in a straight sale of Treasury Bonds on the dates in question.").

Third and finally, Home Concrete "stepped up" its inside basis to equal its partners' artificially inflated outside bases. J.A. 150. Specifically, Home Concrete increased its basis to include the $7.47 million in capital contributions, minus $1.49 million to account for excess basis greater than the fair market value of the partnership's assets. See J.A. 151. The result was a wholly artificial increase of $5.98 million in Home Concrete's inside basis. When Home Concrete sold its assets for $10.62 million, it should have deducted its actual basis of $4.54 million and reported a capital gain of more than $6 million. See J.A. 143, 151. Because Chandler and Pierce (and his trusts) would have been taxed on 19% and 81% of that capital gain, respectively, they would have realized additional taxable income of $1.13 and $4.85 million. See J.A. 129, 158, 162, 166, 170. Instead, Home Concrete deducted its artificially inflated basis of $10.53 million and reported a modest gain of only $69,125. See Pet. App. 4a. As a result, Chandler and Pierce reported adjusted gross income of only $283,618 and $625,445. See J.A. 189, 217.

c. By understating their gain from the sale of Home Concrete in the manner described above, respondents "omit[ted] from gross income an amount properly includible therein." 26 U.S.C. 6501(e)(1)(A). The verb "omit" most commonly means "to leave out or leave unmentioned[;] fail to insert, include, or name." See *Webster's Third New International Dictionary of the English Language* 1574 (1993); see *Webster's New International Dictionary of the English Language* 1700 (2d ed. 1958) (defining "omit" as "[t]o leave out or unmentioned; not to insert, include, or name"); see also *The American Heritage Dictionary of the English Language* 1227 (4th ed. 2006) (same; "[t]o fail to include or mention; leave

out"); *The New Shorter Oxford English Dictionary on Historical Principles* 1994 (4th ed. 1993) (same; "[l]eave out; fail to include"); cf. *Black's Law Dictionary* 1197 (9th ed. 2009) (defining "omission" in part as "[t]he act of leaving something out" or "[s]omething that is left out").

If respondents had accurately stated their bases in Home Concrete before subtracting those bases from its sales price, they would have reported taxable capital gains totaling approximately $6 million. The difference between that sum and the gains respondents actually reported is naturally characterized as an "amount" that was "properly includible" (*i.e.*, that ought to have been included) in respondents' "gross income," but that respondents instead "le[ft] out" or "omit[ted]." As the Seventh Circuit has explained, "an improper inflation of basis is definitively a 'leav[ing] out' from 'any income from whatever source derived' of a quantitative 'amount' properly includible." *Beard* v. *Commissioner*, 633 F.3d 616, 622 (7th Cir. 2011) (brackets in original), petition for cert. pending, No. 10-1553 (filed June 23, 2011). That court correctly reasoned that "[t]here is an amount—the difference between the inflated and the actual basis—which has been left unmentioned on the face of the tax return as a candidate for inclusion in gross income." *Ibid.*

Respondents omitted an amount from their gross income by overstating their bases in Home Concrete, no less than if they had understated the partnership's sale price. Because a taxpayer's gross income (*i.e.*, the portion of his income that is taxable) from a property sale is determined by deducting his basis in the asset from its sale price, either type of misrepresentation will have exactly the same practical effect of misleading the IRS

with respect to the amount of gain (and thus the amount of federal income-tax liability) that is attributable to the sale. Here, respondents reported a total capital gain of $69,125—even though their actual capital gain was more than $6 million. Respondents thus concealed approximately $6 million in income that they had derived from the sale of Home Concrete, no less than if they had misrepresented the partnership's sale price.

2. Adjacent statutory provisions reinforce the inference that an overstatement of basis can trigger the extended six-year assessment period

Two adjacent provisions within Section 6501(e) reinforce the understanding that the phrase "omits from gross income an amount properly includible therein" encompasses understatements of income that are attributable to overstatements of basis.

a. Following the principal paragraph of Section 6501(e)(1)(A) at issue here, subparagraphs (i) and (ii) set forth two exceptions to the general rule. The first of those exceptions states that "[i]n the case of a trade or business, the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services * * * prior to diminution by the cost of such sales or services." 26 U.S.C. 6501(e)(1)(A)(i). Thus, for a trade or business, gross income from the sale of goods or services is simply the sale price, without the offset for the seller's basis that is used to determine the gross income of non-trade-or-business taxpayers.[6]

---

[6] The second exception states that "[i]n determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted * * * if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item."

The principal effect of subparagraph (i) is to eliminate the possibility that a trade or business could trigger the six-year assessment period by overstating its basis in sold property. That special rule for trades and businesses would be unnecessary if, as respondents contend, the phrase "omits from gross income an amount properly includible therein" *already* excluded understatements of income attributable to overstatements of basis. See *Intermountain Ins. Serv. of Vail, LLC* v. *Commissioner*, 650 F.3d 691, 704 (D.C. Cir. 2011) (*Intermountain*) ("Because Intermountain's interpretation of [S]ection 6501(e)(1)(A)'s principal paragraph would accomplish exactly the same result but for all taxpayers, including those engaged in a trade or business, its interpretation renders [subparagraph] (i) largely redundant."); *Beard*, 633 F.3d at 622 ("If the omissions from gross income contemplated by Section 6501(e)(1)(A) were only specific items such as receipts and accruals, then the special definition in [subpara-

---

26 U.S.C. 6501(e)(1)(A)(ii). Subparagraph (ii) thus provides that an omission from gross income will not trigger the six-year assessment period if the taxpayer's return (or a statement attached to the return) adequately apprises the IRS of information from which the omitted amount can be ascertained. Subparagraph (ii) is not at issue in this Court. Although respondents sought to invoke subparagraph (ii) in the district court, the court found that respondents' returns did not sufficiently disclose their true gains from the sale of Home Concrete. See J.A. 106 ("[P]laintiffs' returns contain misleading statements and information that obscured the substance of the disputed underlying transactions."); J.A. 110 ("[E]ven an IRS examiner trained in the art of divination would have been hard pressed to discern plaintiffs' true actions."); pp. 25-26, *infra*. And while the court of appeals stated that "Home Concrete's 1999 tax return reported the basic components of the transactions," Pet. App. 4a, it did not suggest that respondents satisfied the requirements of subparagraph (ii).

graph] (i) would be, if not superfluous, certainly diminished."). The most natural inference is that "Congress understood the 'omits from gross income' language to include basis overstatements and added [subparagraph] (i) as an exception limited to the trade or business context." *Intermountain*, 650 F.3d at 704.

To be sure, respondents' interpretation would not render subparagraph (i) entirely superfluous. Both for a trade or business and for any other taxpayer, the applicability of the six-year assessment period depends on whether the taxpayer has omitted an amount of gross income "in excess of 25 percent of the amount of gross income stated in the return." 26 U.S.C. 6501(e)(1)(A). In addition to making clear that a trade or business cannot trigger the extended assessment period by overstating its basis in property, subparagraph (i), by specifying that the "gross income" of a trade or business from a property sale is simply the sale price, alters the denominator to which the "25 percent" requirement is applied. See *Salman Ranch Ltd* v. *United States*, 573 F.3d 1362, 1375 (Fed. Cir. 2009) (*Salman Ranch I*); *Bakersfield Energy Partners, LP* v. *Commissioner*, 568 F.3d 767, 776-777 (9th Cir. 2009).

As the District of Columbia Circuit has explained, however, Congress added subparagraph (i) "amidst a debate that had divided the courts of appeals and that specifically revolved around whether basis overstatements constituted omissions from gross income." *Intermountain*, 650 F.3d at 704-705; see pp. 45-46, *infra*. Although respondents' construction of Section 6501(e)(1)(A) would not deprive subparagraph (i) of all practical effect, it would render that subparagraph irrelevant to the issue that had spawned a circuit split, reducing it to a minor tweak in the formula used to deter-

mine the applicability of the six-year assessment period. That reading ignores the historical backdrop against which Congress acted and the nature of the problem that subparagraph (i) was intended to address. See *Babbitt* v. *Sweet Home Chapter of Cmtys. for a Great Or.*, 515 U.S. 687, 701 (1995) ("When Congress acts to amend a statute, we presume it intends its amendment to have real and substantial effect.") (internal quotation marks and citation omitted).

b. Section 6501(e)(2), which applies to estate and gift taxes, gives the IRS six years from the filing of a return to assess additional tax "if the taxpayer omits * * * *items* includible" in the gross estate. 26 U.S.C. 6501(e)(2) (emphasis added). Congress used the term "items" to "make[] it clear that the [six]-year period is not to apply merely because of differences between the taxpayer and the Government as to the valuation of property." Staff of the Joint Comm. on Internal Revenue Taxation, 84th Cong., 1st Sess., *Summary of the New Provisions of the Internal Revenue Code of 1954*, at 130 (Comm. Print 1955).

By contrast, Section 6501(e)(1)(A) provides for a six-year assessment period "[i]f the taxpayer omits from gross income an *amount* properly includible therein." 26 U.S.C. 6501(e)(1)(A) (emphasis added). Congress's reference to "amount[s]" rather than "items" strongly suggests that the six-year assessment period "applies both in cases where an item of income is completely left out and in situations where the amount of gross income reported is understated due to an error in the calculation." *Brandon Ridge Partners* v. *United States*, No. 8:06-cv-1340, 2007 WL 2209129, at *7 (M.D. Fla. July 30, 2007). In either case, "an amount" of gross income has been omitted from the return. And once that

proposition is established, the statutory text provides no basis for distinguishing between (i) understatements of gross income that are attributable to understatements of receipts and (ii) those that are attributable to overstatements of basis.

3. The statutory purpose strongly supports extending the period for discovery of a basis overstatement

Section 6501(e)(1)(A)'s language must be interpreted in light of Congress's reasons for extending the assessment period in cases involving omissions from gross income. See *Dolan* v. *USPS*, 546 U.S. 481, 486 (2006) (statutory interpretation requires courts to "read[] the whole statutory text, consider[] the purpose and context of the statute, and consult[] any precedents or authorities that inform the analysis"); *United States* v. *Heirs of Boisdoré*, 49 U.S. (8 How.) 113, 122 (1849). The evident rationale for extending the assessment period in cases involving substantial omissions from gross income is that such omissions are often difficult to detect. Unlike (for example) a potentially improper deduction, which provides a natural trigger for IRS inquiry, an omitted amount of gross income does not appear on the face of the taxpayer's return, and it may take considerable time and effort for the government to discover from other sources of information that the taxpayer has received greater income than he reported. Congress's focus on the adequacy of notice to the IRS is confirmed by Section 6501(e)(1)(A)(ii), which provides that an omitted amount will not trigger the extended assessment period if either the taxpayer's return or an attached statement contains information "adequate to apprise the Secretary of the nature and amount of [the omitted] item." The cases to which the six-year assessment period applies

thus by definition involve returns that do *not* adequately apprise the IRS of the omitted amounts.

The rationale for Section 6501(e)(1)(A) is fully applicable to a case in which the taxpayer overstates his basis in property, because a basis overstatement will typically be at least as difficult to detect as an understatement of the property's sale price. The government has no immediate means of discerning from the face of a return that a taxpayer has underreported his gross income by (i) overstating what he invested in the property's acquisition or (ii) understating what he received in the property's divestment. In either instance, extending the assessment period from three to six years allows the government sufficient time to investigate the asset basis and sale price, and it thereby decreases the likelihood that a taxpayer will defeat his tax obligations by understating his gross income.

The circumstances of this case aptly illustrate the difficulties of detecting tax-avoidance schemes that operate through overstatements of basis in sold property. If respondents had not engaged in the Son-of-BOSS transactions, the $10.6 million sale of Home Oil would have generated a taxable capital gain of approximately $6 million (because the taxpayers' existing bases in Home Oil totaled approximately $4.5 million). Respondents therefore created Home Concrete as a vehicle for the Son-of-BOSS transactions, transferred Home Oil's assets to Home Concrete, engaged in short sales that artificially inflated their bases in Home Concrete by a total of $5.98 million, and then reported modest gains from Home Concrete's sale. See pp. 16-18, *supra*. None of respondents' returns, however, disclosed that the reason for the high bases was the taxpayers' asymmetric treatment of the short sales.

Indeed, respondents' returns did not even provide adequate notice of the short sales themselves, let alone their connection to the inflated bases. In the district court, respondents sought to invoke the safe harbor in Section 6501(e)(1)(A)(ii), arguing that they had disclosed the substance of the transactions in their returns. As the district court explained in rejecting that argument, "[n]othing about the disclosure on Pierce and Chandler's individual tax returns reasonably indicates that the opening of the short sales was related to the basis step-up by Home Concrete." J.A. 107. To the contrary, the court observed, "[t]he statement on Pierce and Chandler's tax returns indicates that those taxpayers retained the obligation to close the short sales they had opened. There is no hint that either taxpayer had transferred the obligation to close the short sale." *Ibid.*

With respect to Home Concrete's return, the district court explained that the disclosure "of a sale of Treasury Bonds in Home Concrete's Schedule D also serves as a smokescreen for [respondents'] actual activities." J.A. 107. Respondents "did not disclose a 'short sale' of Treasury Bonds or the 'close of a short sale position,' nor did they use any other descriptive moniker that accurately described the transaction." J.A. 108. Rather, respondents' description of the transaction conveyed the "misleading[]" impression that "they were reporting a straight sale of Treasury Bonds instead of the back-end of a short sale transaction." J.A. 108-109; see J.A. 109 ("[T]he only reasonable conclusion a reviewer was likely to draw was that Home Concrete engaged in a straight sale of Treasury Bonds on the dates in question."). As the district court observed, "even an IRS examiner trained in the art of divination would have been

hard pressed to discern [respondents'] true actions." J.A. 110.

This case thus illustrates why a basis overstatement that is not adequately disclosed on a taxpayer's return can be extremely difficult to detect and warrants application of the extended six-year period in Section 6501(e)(1)(A). The court of appeals' contrary holding would reward taxpayers who evade detection by the government within Section 6501(a)'s three-year assessment period by overstating their bases in property in complicated ways. See Bernard J. Audet, Jr., Note, *One Case To Rule Them All: The Ninth Circuit in* Bakersfield *Applies* Colony *To Deny the IRS an Extended Statute of Limitations in Overstatement of Basis Cases*, 55 Vill. L. Rev. 409, 432-433 (2010) (noting that the court of appeals' approach "allow[s] tax shelter abusers to escape tax liability by disclosing the amounts of their transactions but concealing the substance, nature, origin, and destination of those amounts in ways that put the Service at a disadvantage in detecting noncompliance").

B. The Recent Treasury Regulation Resolves Any Statutory Ambiguity By Specifying That An Overstatement Of Basis Triggers The Six-Year Assessment Period

To the extent that the statutory language is ambiguous, the Department of the Treasury has recently promulgated a regulation, Treas. Reg. 301.6501(e)-1, that resolves the question presented here. The regulation states that an understatement of gross income attributable to an overstatement of basis in property is an "omi[ssion] from gross income" that triggers the six-year assessment period in 26 U.S.C. 6501(e)(1)(A). See Pet. App. 67a-72a. That regulation was validly promul-

gated, applies to this case, is entitled to deference, and is not impermissibly retroactive.

1. The final regulation was validly promulgated

a. In September 2009, the Treasury Department issued a temporary regulation to address the application of Section 6501(e)(1)(A) to cases involving overstatements of taxpayers' bases in property. See T.D. 9466, 2009-43 I.R.B. 551 (issuing Temp. Treas. Reg. 301.6501(e)-1T (2009)). The regulation provided that, "as it relates to any income other than from the sale of goods or services in a trade or business," "gross income means the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property." Temp. Treas. Reg. 301.6501(e)-1T(a)(1)(iii) (2009) (emphasis omitted). "Consequently," the regulation explained, "an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of [S]ection 6501(e)(1)(A)." *Ibid.*

At the same time that it issued the temporary regulation, the Treasury Department issued a notice of proposed rulemaking with a 90-day comment period for an identical final regulation. See 74 Fed. Reg. 49,354 (Sept. 28, 2009). In December 2010, the Department withdrew the temporary regulation and issued the final regulation that is currently in effect. See T.D. 9511, 2011-6 I.R.B. 455 (Pet. App. 57a-72a). The text of the final regulation tracks the temporary regulation in virtually every respect. In particular, like the temporary regulation, the final regulation states that "an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from

gross income for purposes of [S]ection 6501(e)(1)(A)(i)." Treas. Reg. 301.6501(e)-1(a)(1)(iii).

During the comment period, the Treasury Department received a single comment, which characterized the regulation as having "retroactive effect 'in that taxable years which had closed are now reopened.'" Pet. App. 62a (quoting comment). Responding to that comment in the preamble to the final regulation, the Department "disagree[d] with the characterization of the regulations as retroactive" and noted that "[t]he final regulations have been clarified to emphasize that they only apply to open tax years, and do not reopen closed tax years." *Ibid.* The Department amended the regulation's applicability clause to state that the regulation "applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009," *i.e.*, the effective date of the regulation. Treas. Reg. 301.6501(e)-1(e)(1). There was no other relevant change from the temporary regulation to the final regulation.

b. In the court of appeals, respondents and their amicus (Bausch & Lomb Incorporated) challenged the temporary regulation as procedurally invalid under the Administrative Procedure Act (APA), 5 U.S.C. 553, on the ground that it had been adopted without following notice-and-comment procedures. See Resp. C.A. Reply Br. 9-16; Amicus C.A. Br. 11-15. That argument was incorrect. See 26 U.S.C. 7805(e)(1) (granting the Treasury Department authority to issue temporary regulations); see also Gov't C.A. Br. 38-42. In any event, the prior dispute concerning the validity of the temporary regulation is irrelevant to the proper disposition of this case. In December 2010, after following notice-and-comment procedures, the Department withdrew the temporary regulation and replaced it with the current

final rule. See *Intermountain*, 650 F.3d at 709. The final regulation was therefore in effect when the court of appeals decided this case, and it continues to be in effect today.

In other cases, respondents' amicus has argued that the Department "failed to keep an 'open mind' during the notice-and-comment period." *Intermountain*, 650 F.3d at 709. As the District of Columbia Circuit explained in rejecting that argument, open-mindedness review "[o]rdinarily" applies only when an agency "issues final regulations without the requisite comment period and then tries to cure that [APA] violation by holding a post-promulgation comment period." *Ibid.* "Even assuming the applicability of this framework" when an agency issues a temporary regulation, holds a comment period, and then issues a final regulation, the Department's "searching consideration" of the single comment received during the comment period leaves "no doubt that [it] kept the requisite open mind." *Id.* at 709-710 (internal quotation marks and citation omitted).

2. The final regulation applies to this case

a. By its terms, the final regulation "applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009." Treas. Reg. 301.6501(e)-1(e). As the Treasury Department explained in the preamble to the final rule, "[t]he expiration of the three-year period does not 'close' a taxable year if a longer period applies." Pet. App. 63a. "Consistent with that position," the Department further explained, "the final regulation[] appl[ies] to taxable years with respect to which the six-year period for assessing tax under [S]ection * * * 6501(e)(1) was open on or after September 24, 2009." *Ibid.* That includes "all tax-

able years (1) for which six years had not elapsed from the later of the date that a tax return was due or actually filed [or] (2) that are the subject of any case pending before any court of competent jurisdiction (including the United States Tax Court and Court of Federal Claims) in which a decision had not become final (within the meaning of [S]ection 7481)." *Ibid.*; see *Intermountain*, 650 F.3d at 709 ("[T]he Commissioner announced his definitive interpretation in the preamble to the final regulations.").[7]

This case falls within the second category identified in the preamble. In September 2006, the IRS issued a Final Partnership Administrative Adjustment (FPAA) contesting the accuracy of Home Concrete's partnership return. Pet. App. 4a-5a. As of September 24, 2009, respondents' current challenge to the FPAA was "the subject of [a] case pending before [a] court of competent jurisdiction * * * in which a decision had not become final." *Ibid.*; see 26 U.S.C. 7481(a) (decisions of Tax Court become final when time for seeking further review expires); 26 U.S.C. 6230(g) (finality of district court and Court of Federal Claims decisions is determined in accordance with "the principles of section 7481(a)"). The preamble thus makes clear that, in resolving respondents' challenge to the FPAA—and, in particular, in determining whether the FPAA was timely issued—the courts should apply the final regulation's definition of the phrase "omits from gross income an amount properly includible therein."

---

[7] The final regulation also applies to taxable years for which tax liability had not become fixed pursuant to a settlement between the IRS and the taxpayer. See Pet. App. 63a; see also 26 U.S.C. 7121. That application of the regulation is not at issue here.

That interpretation of the Treasury Department's own regulation is "controlling" because it is not "plainly erroneous or inconsistent with the regulation." *Pliva, Inc.* v. *Mensing*, 131 S. Ct. 2567, 2575 (2011) (quoting *Auer* v. *Robbins*, 519 U.S. 452, 461 (1997)); see *Kennedy* v. *Plan Adm'r for DuPont Sav. & Inv. Plan*, 555 U.S. 285, 295-296 (2009) (deferring to the Treasury Department's interpretation of its regulation). Even assuming that there are "other ways to interpret the regulation[]," the Department's interpretation is a permissible one, and it represents the Department's "fair and considered judgment" on the meaning of Section 6501(e)(1)(A). *Mensing*, 131 S. Ct. at 2575.

Other courts of appeals to consider the question—the Federal, Tenth, and District of Columbia Circuits—have held that the regulation applies to pending cases like this one. See *Grapevine Imports, Ltd.* v. *United States*, 636 F.3d 1368, 1383 (Fed. Cir. 2011) ("[B]y their plain terms the new Treasury regulations apply to Grapevine's 1999 return.") (*Grapevine*), petition for cert. pending, No. 11-163 (filed Aug. 5, 2011); *Salman Ranch Ltd.* v. *United States*, 647 F.3d 929, 942 (10th Cir. 2011) (*Salman Ranch II*) ("[T]he preamble to the final regulation makes clear that the regulation applies to taxpayers in the Partnership's position."), petition for cert. pending, No. 11-582 (filed Nov. 7, 2011); *ibid.* ("The straightforward application of these provisions leaves no doubt the Partnership's 2001 and 2002 tax years were open on September 24, 2009 and remain so today."); *Intermountain*, 650 F.3d at 709 (concluding that although the applicability clause is "fairly cryptic," "[the Commissioner's] interpretative solution is neither plainly erroneous nor inconsistent with the regulation"); but see *Burks* v. *United States*, 633 F.3d 347, 360 (5th Cir.

2011), petition for cert. pending, No. 11-178 (filed Aug. 11, 2011).

b. The court of appeals stated that, "[e]ven assuming *arguendo* that the six-year statute of limitations applied, pursuant to the regulation, the 'period for assessing tax' would have expired, according to the district court's unchallenged finding, on September 14, 2006." Pet. App. 13a; see note 5, *supra*. The court therefore concluded that "the period for assessing tax for the 1999 tax year expired long before September 24, 2009," and that the final regulation (which applies by its terms "to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009") was therefore inapplicable to this case. Pet. App. 13a. The court of appeals' analysis reflects a basic misunderstanding of the statutory scheme that governs the assessment of additional tax against individual partners.

When the IRS disagrees with information reported on a partnership's return, including its reported gross income, the IRS issues an FPAA to the partners. See *UTAM, Ltd.* v. *Commissioner*, 645 F.3d 415, 419 (D.C. Cir. 2011) (*UTAM*). That FPAA is not itself an assessment of additional tax; rather, the partnership's "tax matters partner" (or certain other partners) may contest the FPAA in a judicial proceeding before any additional tax is assessed against the individual partners. See 26 U.S.C. 6223(a); *UTAM*, 645 F.3d at 419. The timely issuance of an FPAA suspends the running of the applicable assessment period for any individual partner. See 26 U.S.C. 6229(d); see also *UTAM*, 645 F.3d at 419-420; *Epsolon Ltd.* v. *United States*, 78 Fed. Cl. 738, 761-762 (2007); *Rhone-Poulenc Surfactants & Specialties, L.P.* v. *Commissioner*, 114 T.C. 533, 554 (2000), appeal dismissed, 249 F.3d 175 (3d Cir. 2001). That toll-

ing rule ensures that the time to assess additional tax against individual partners does not expire while the partnership contests the FPAA.

The IRS has not assessed additional taxes against respondents, and it will not do so unless and until the FPAA is finally upheld against respondents' timeliness challenge and the adjustments in the FPAA are sustained. But if the FPAA is sustained, the IRS remains free to assess additional tax against Home Concrete's individual partners in a manner consistent with the partnership-level adjustments set forth in the FPAA. The court of appeals was therefore wrong in stating that "the 'period for assessing tax' * * * expired * * * on September 14, 2006." Pet. App. 13a. Although the period for assessing tax *would have* expired on that date if the FPAA had not been issued, the timely issuance of the FPAA suspended the period for assessing tax against the individual partners.

c. Respondents suggest (Br. in Opp. 25-26) that, to determine whether the Treasury regulation applies to this case, the Court must decide *without reference to the regulation itself* whether "the period for assessing tax was open on or after September 24, 2009." Treas. Reg. 301.6501(e)-1(e)(1). On respondents' view, the better reading of Section 6501(e)(1)(A) is that an overstatement of basis cannot trigger the six-year assessment period. On that theory, the correct assessment period was three years; the three-year period closed well before the September 2006 issuance of the FPAA; and thus the Treasury regulation is inapplicable to this case. Respondents' approach to determining the applicability of the rule is wrong for at least three reasons.

First, the final regulation's applicability clause and its substantive provisions must be read together as a

coherent whole. Cf., *e.g.*, *Robinson* v. *Shell Oil Co.*, 519 U.S. 337, 341 (1997) (Statutory interpretation requires "reference to the language itself, the specific context in which that language is used, and the broader context of the statute as a whole."). Thus, in determining (for purposes of the applicability clause) whether "the period for assessing tax" in a particular case "was open on or after September 24, 2009," the Court should adopt the understanding of the phrase "omits from gross income an amount properly includible therein" that is set forth in other provisions of the same final rule. Respondents, by contrast, urge the Court to utilize a *different* interpretation of that phrase—indeed, the very interpretation that the final rule was intended to reject—in construing the regulation's applicability clause. That approach would render the regulation self-defeating and is inconsistent with basic canons of construction.

Second, the preamble to the final regulation confirms the most natural reading of the regulation's text. In the preamble, the Treasury Department expressly disagreed with the interpretation of the applicability clause—adopted by the Tax Court in *Intermountain Ins. Serv. of Vail, LLC* v. *Commissioner*, 134 T.C. 211, 219-220 (2010), but subsequently rejected by the District of Columbia Circuit on appeal, see *Intermountain*, 650 F.3d at 708-709—that respondents advance in this Court. See Pet. App. 63a ("The Tax Court's majority in *Intermountain* erroneously interpreted the applicability of the temporary and proposed regulations."). The Department explained that, in determining whether the "period for assessing tax * * * was open on or after September 24, 2009," the relevant "period for assessing tax" in cases involving basis overstatement is six rather than three years because "[t]he expiration of the three-

year period does not 'close' a taxable year if a longer period applies." *Ibid.*; see *Intermountain*, 650 F.3d at 708 ("[B]ecause the pre-regulation state of the law was neither settled nor clear, the Commissioner could reasonably read each of the regulations' provisions, including the applicability provision, in light of the others."). The Department further explained that the final regulation applies to, *inter alia*, "all taxable years * * * that are the subject of any case pending before any court of competent jurisdiction * * * in which a decision had not become final" as of September 24, 2009. Pet. App. 63a. The preamble thus clearly resolves any ambiguity that might be present in the text of the applicability clause.

Third, an important purpose of the final rule was to clarify the proper resolution of several pending cases in which the choice between the three- and six-year assessment periods was likely to be dispositive. The preamble to the final rule observed that "[t]he interpretation of the phrase 'omits from gross income' as used in section 6501(e)(1) is currently pending before several United States Courts of Appeals," Pet. App. 61a, and stated that the rule would apply to cases pending in court on or after September 24, 2009, *id.* at 63a. As the District of Columbia Circuit concluded after surveying the regulatory history, there is "no doubt that the Commissioner intended from the moment these regulations issued to apply them to cases pending as of September 24, 2009." *Intermountain*, 650 F.3d at 708.

Under respondents' view of the applicability clause, however, the final regulation would be irrelevant not only to this case, but to substantially all the suits that were pending at the time the rule was promulgated. Acceptance of that view would require this Court to re-

solve without the agency's guidance the very interpretive question—whether Section 6501(e)(1)(A) encompasses understatements of gross income that are attributable to overstatements of basis—that the regulation was designed to settle. If the Court treated the regulation as inapplicable and ultimately agreed with respondents that Section 6501(e)(1)(A) is better read not to encompass such understatements, the Court's decision would not definitively resolve the issue. Rather, the lower courts would then be required to entertain an additional round of suits to decide the validity of the regulation in later cases to which the rule unquestionably applies (*i.e.*, those in which even the three-year assessment period remained open on September 24, 2009). See *National Cable & Telecomms. Ass'n* v. *Brand X Internet Servs.*, 545 U.S. 967, 982-983 (2005) (*Brand X*) ("Only a judicial precedent holding that the statute unambiguously forecloses the agency's interpretation, and therefore contains no gap for the agency to fill, displaces a conflicting agency construction."). In clarifying that the regulation applies to pending cases, the Treasury Department sought to obviate the need for such duplicative litigation.

3. The final regulation is entitled to deference

To the extent that Section 6501(e)(1)(A) is ambiguous with respect to the question presented here, the Treasury regulation resolves that ambiguity. The Treasury Department's interpretation of the statute that it administers is reasonable and entitled to deference under *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837 (1984) (*Chevron*).

a. Last Term in *Mayo Foundation for Medical Education & Research* v. *United States*, 131 S. Ct. 704 (2011)

(*Mayo*), this Court confirmed that "[t]he principles underlying [its] decision in *Chevron* apply with full force in the tax context." *Id.* at 713. As the Court explained, "[f]illing gaps in the Internal Revenue Code plainly requires the Treasury Department to make interpretive choices for statutory implementation at least as complex as the ones other agencies must make in administering their statutes." *Ibid.* (citing *Bob Jones Univ.* v. *United States*, 461 U.S. 574, 596 (1983) ("In an area as complex as the tax system, the agency Congress vests with administrative responsibility must be able to exercise its authority to meet changing conditions and new problems.")). The Court therefore saw "no reason why [its] review of tax regulations should not be guided by agency expertise pursuant to *Chevron* to the same extent as [its] review of other regulations." *Ibid.*

Here, as in *Mayo*, the Treasury Department has promulgated a regulation pursuant to its general authority under Section 7805(a) to "prescribe all needful rules and regulations for the enforcement" of the Internal Revenue Code. 26 U.S.C. 7805(a); see *Mayo*, 131 S. Ct. at 713. Here, as in *Mayo*, the Department issued the regulation after conducting notice-and-comment procedures. See *id.* at 714. And here, as in *Mayo*, the regulation "easily satisfies the second step of *Chevron*, which asks whether the Department's rule is a 'reasonable interpretation' of the enacted text." *Ibid.* (quoting *Chevron*, 467 U.S. at 844); see *id.* at 711 (noting that under *Chevron*'s second step, courts "may not disturb an agency rule unless it is arbitrary or capricious in substance, or manifestly contrary to the statute") (internal quotation marks and citation omitted). For all of the reasons set forth in Part A, *supra*, treating an understatement of gross income attributable to an overstatement of basis

in property as an "omi[ssion] from gross income" comports with the statutory text, structure, and purpose.

Accordingly, every court of appeals to reach *Chevron*'s second step has held that the regulation is reasonable and entitled to deference. See *Intermountain*, 650 F.3d at 707 ("Arriving at last at *Chevron* step two, our task is easy. * * * [W]e see nothing unreasonable in the Commissioner's decision to diverge from *Colony*'s holding."); *Salman Ranch II*, 647 F.3d at 940 ("Several factors lead us to conclude the IRS's interpretation is reasonable and not arbitrary or capricious."); *ibid.* (observing that the IRS's interpretation of "gross income" in Section 6501(e)(1)(A) "is consistent with the definition of 'gross income' used elsewhere in the Tax Code" and "is consistent with legislative history suggesting Congress enacted the 'gross receipts' provision of subparagraph (i) as an exception to the general definition of 'gross income'"); *Grapevine*, 636 F.3d at 1381 ("Because the Treasury regulations are a reasonable interpretation of [Section] 6501(e)(1)(A), they must receive our deference."); but see *Burks*, 633 F.3d at 360-361 n.9 (holding that the statute is unambiguous but suggesting that "it is unclear whether the [r]egulations would be entitled to *Chevron* deference under *Mayo*").

b. Respondents' amicus argues that "the fact that the Commissioner promulgated these regulations in the midst of pending litigation, to effectively reverse judicial decisions that were running very strongly in the taxpayers' favor, raises very difficult questions under * * * the *Chevron* doctrine." Bausch & Lomb Amicus Cert. Br. 17. That argument is misconceived. This Court "has made crystal clear that it is utterly 'irrelevant' to the question of whether *Chevron* deference is due '[t]hat it was litigation which disclosed the need for the regula-

tion.'" *Intermountain*, 650 F.3d at 706 (brackets in original) (quoting *Smiley* v. *Citibank (S.D.), N.A.*, 517 U.S. 735, 741 (1996)). Indeed, just this past Term in *Mayo*, this Court "found it immaterial to [its] analysis that a regulation was prompted by litigation." 131 S. Ct. at 712 (internal quotation marks omitted). Nor does it matter that the Treasury Department, having lost in some lower courts, promulgated its regulation in part to reverse those judicial decisions. Confronting exactly that scenario in *United States* v. *Morton*, 467 U.S. 822 (1984), this Court reasoned that even "assuming the promulgation of [the regulation] was a response to this suit, that demonstrates only that the suit brought to light an additional administrative problem of the type that Congress thought should be addressed by regulation." *Id.* at 836 n.21.

4. The final regulation is not impermissibly retroactive

Respondents argue that the Treasury regulation has an impermissible retroactive effect. See Br. in Opp. 27-28. That is incorrect for several reasons.

a. The regulation is not retroactive in the relevant sense because it clarified rather than changed existing law. "[W]here a new rule constitutes a clarification—rather than a substantive change—of the law as it existed beforehand, the application of that new rule to pre-promulgation conduct necessarily does *not* have an impermissible retroactive effect." *Levy* v. *Sterling Holding Co.*, 544 F.3d 493, 506 (3d Cir. 2008), cert. denied, 129 S. Ct. 2827 (2009). That is because, as the Seventh Circuit has explained, "[a] rule simply clarifying an unsettled or confusing area of the law * * * does not change the law, but restates what the law according to the agency is and has always been: 'It is no more retro-

active in its operation than is a judicial determination construing and applying a statute to a case in hand.'" *Pope* v. *Shalala*, 998 F.2d 473, 483 (7th Cir. 1993) (quoting *Manhattan Gen. Equip. Co.* v. *Commissioner*, 297 U.S. 129, 135 (1936)), overruled on other grounds by *Johnson* v. *Apfel*, 189 F.3d 561 (7th Cir. 1999). Accordingly, where "a court is addressing transactions that occurred at a time when there was no clear agency guidance, it would be absurd to ignore the agency's current authoritative pronouncement of what the statute means." *Smiley*, 517 U.S. at 744 n.3.

Here, it was not settled at the time of the Treasury regulation whether *Colony*'s interpretation of the pre-1954 version of the statute applies equally to the post-1954 version of the statute (as respondents maintain) or whether instead the 1954 amendments affect the statutory analysis (as the government has argued). See *Intermountain*, 650 F.3d at 709 ("Because *Colony* never applied to [S]ection 6501(e)(1)(A) * * *, there was no *settled* law for the regulations to change."); *CC & F W. Operations Ltd. P'ship* v. *Commissioner*, 273 F.3d 402, 406 n.2 (1st Cir. 2001) ("Whether *Colony*'s main holding carries over to [S]ection 6501(e)(1) is at least doubtful."). The regulation therefore clarified a point that was previously unresolved by codifying the interpretation of Section 6501(e)(1)(A) that the Treasury Department had consistently advanced in prior adjudicative proceedings.

b. The fact that the regulation does not bear on the legality of petitioners' primary conduct further supports the conclusion that it is not retroactive in the relevant sense. The regulation does not speak to the question whether respondents overstated their bases in Home Concrete and consequently underpaid their taxes.

Rather, it clarifies the procedural rules governing enforcement of respondents' pre-existing tax liabilities. This Court has "generally applied new procedural rules to pending cases * * * because rules of procedure regulate secondary rather than primary conduct." *Lindh* v. *Murphy*, 521 U.S. 320, 341 (1997) (internal quotation marks and citation omitted); cf. *Landgraf* v. *USI Film Prods.*, 511 U.S. 244, 275 (1994) ("Because rules of procedure regulate secondary rather than primary conduct, the fact that a new procedural rule was instituted after the conduct giving rise to the suit does not make application of the rule at trial retroactive.").

c. Even if the regulation were properly viewed as retroactive, the Treasury Department has express statutory authority to promulgate retroactive rules. See *Bowen* v. *Georgetown Univ. Hosp.*, 488 U.S. 204, 209 (1988) (permitting retroactive rulemaking when there is an "express statutory grant" of such power). The relevant statute, 26 U.S.C. 7805(b)(8), authorizes the Treasury Department to "prescribe the extent, if any, to which any * * * regulation relating to the internal revenue laws shall be applied without retroactive effect." In light of Section 7805(b)(8), this Court has recognized the Department's authority to apply a regulation retroactively, subject to review for abuse of the Department's discretion. See *Automobile Club* v. *Commissioner*, 353 U.S. 180, 184 (1957) (discussing 26 U.S.C. 3791(b) (1940), which was the predecessor statute to Section 7805(b)(8)) ("[I]t is clear from the language of [Section 7805(b)(8)] and its legislative history that Congress thereby confirmed the authority of the Commissioner to correct any ruling, regulation or Treasury decision retroactively.") (footnote omitted).

In the final regulation, "[t]he Treasury Department and the Internal Revenue Service disagree[d] with the characterization of the regulation[] as retroactive." Pet. App. 62a. The Department also observed, however, that "a retroactive regulation interpreting * * * [Section] 6501(e)(1) is expressly permitted by the applicable version of [S]ection 7805(b)." *Id.* at 62a-63a; see *id.* at 62a (explaining why 1996 amendments to Section 7805(b) do not alter the Department's authority to make the final regulation at issue here retroactive); *Grapevine*, 636 F.3d at 1381 n.6 (same). The Department thus made clear that, to the extent the final regulation has any retroactive effect, the regulation is a permissible exercise of the Department's authority to promulgate retroactive rules.

The court below did not consider these arguments, but other courts of appeals have held that the regulation is not impermissibly retroactive. See *Salman Ranch II*, 647 F.3d at 943 ("We agree with the Federal Circuit that the new regulation may be properly applied to past tax years whose limitations periods remain open as recomputed under the new regulation."); *Grapevine*, 636 F.3d at 1382 ("By their terms, the new regulations will apply only to those taxpayers who are within the limitations period as computed under the new regulation, so there is no opportunity for these regulations to reach into the distant past."); *ibid.* ("[W]hile we recognize that some taxpayers whose past returns bear evidence of overstated basis may find themselves facing adjustments when they thought the limitations period had lapsed, we cannot say that the burden on those taxpayers is so great as to be an abuse of the Treasury Department's discretion.").

C. This Court's Decision In *Colony* Does Not Control The Interpretation Of The Current Version Of Section 6501(e)(1)(A)

Respondents contend (Br. in Opp. 28-33) that the regulation is not entitled to *Chevron* deference because it is contrary to this Court's decision in *Colony*. In *Colony*, this Court construed a predecessor statute, 26 U.S.C. 275(c) (1940), that also included the language "omits from gross income an amount properly includible therein." The Court held that former Section 275(c) did not encompass understatements of gross income that were attributable to overstatements of basis. See 357 U.S. at 30, 32, 36-37. Respondents contend that the Court in *Colony* held the language of the former statute to be unambiguous; that the holding in *Colony* applies equally to the current Section 6501(e)(1)(A); and that the IRS is therefore foreclosed from adopting a different construction of the current law. Those arguments lack merit. A careful analysis of the statutory history and the *Colony* decision demonstrates that *Colony* does not control this case. See *Intermountain*, 650 F.3d at 701-706 (discussing the statutory history and the limited scope of *Colony*'s holding).

1. When it amended the relevant statutory provision in 1954, Congress made clear that a basis overstatement triggers the six-year assessment period unless the taxpayer is a trade or business

Congress first established an extended assessment period in 1934 when it enacted Section 275(c). See Revenue Act of 1934, ch. 277, § 275(c), 48 Stat. 745 (26 U.S.C. 275(c) (1934)). Section 275(c) extended the assessment period from three to five years "[i]f the taxpayer omits from gross income an amount properly includible

therein which is in excess of 25 per centum of the amount of gross income stated in the return." 26 U.S.C. 275(c) (1934). The language of Section 275(c) was thus similar to the current Section 6501(e)(1)(A): the extended assessment period applied if a taxpayer "omit-[ted] from gross income an amount properly includible therein" that was more than 25 percent of the gross income stated in the return.

In the 1940s and 1950s, lower courts reached differing conclusions about whether an overstatement of basis could give rise to an "omi[ssion] from gross income" for purposes of Section 275(c). Contrast *Reis* v. *Commissioner*, 142 F.2d 900, 902-903 (6th Cir. 1944) (holding that a basis overstatement could give rise to an omission from gross income), and *American Liberty Oil Co.* v. *Commissioner*, 1 T.C. 386 (1942) (same), with *Uptegrove Lumber Co.* v. *Commissioner*, 204 F.2d 570, 571-573 (3d Cir. 1953) (holding that a basis overstatement could not give rise to an omission from gross income). Although the Third Circuit in *Uptegrove Lumber* recognized "real ambiguity" in Section 275(c), it held (based on the statute's legislative history) that a taxpayer omits an amount from gross income only when the taxpayer fails to report the sale of an item altogether, not when the taxpayer overstates the cost of that item and thus understates gross income from the item's sale. *Ibid.* In a letter to the Senate Finance Committee, attorneys who endorsed the Third Circuit's reasoning urged the Committee to amend Section 275(c) to codify *Uptegrove Lumber*'s holding, and to indicate that the amendments merely clarified existing law. See *Intermountain*, 650 F.3d at 698.

The following year, Congress revised Section 275(c), which it renumbered as Section 6501(e)(1)(A) in the In-

ternal Revenue Code of 1954. Congress lengthened (from five to six years) the assessment period that applies when a taxpayer omits a substantial amount from gross income, and it added two new subparagraphs (i) and (ii) to Section 6501(e)(1)(A). As explained above, see pp. 20-22, *supra*, the first of those subparagraphs is directly relevant here. Subparagraph (i) states that "[i]n the case of a trade or business, the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services * * * prior to diminution by the cost of such sales or services." 26 U.S.C. 6501(e)(1)(A)(i). Subparagraph (i) thus provides that for goods or services sold by a trade or business, gross income is simply the sales price, without any offset for the seller's basis. Both the House and Senate Reports characterized subparagraphs (i) and (ii) as "changes from existing law." See H.R. Rep. No. 1337, 83d Cong., 2d Sess., at A415 (1954); S. Rep. No. 1622, 83d Cong., 2d Sess. 584 (1954).

Subparagraph (i) thus codified the result but not the reasoning in *Uptegrove Lumber*. Although *Uptegrove Lumber* involved a manufacturing corporation, the Third Circuit's analysis did not distinguish between taxpayers who were engaged in a trade or business and those who were not. See *Intermountain*, 650 F.3d at 697-698. In enacting subparagraph (i), by contrast, Congress established a special definition of "gross income" that applies only "[i]n the case of a trade or business." 26 U.S.C. 6501(e)(1)(A)(i). Even with respect to trade-or-business taxpayers, moreover, Congress did not endorse *Uptegrove Lumber*'s conclusion that the phrase "omits from gross income" is naturally read to exclude basis overstatements. Rather, Congress "literally took basis out of [the] equation, redefining 'gross income' to mean

gross receipts rather than gross receipts minus the cost of goods sold." *Intermountain*, 650 F.3d at 697. By contrast, it is undisputed that respondents' bases in Home Concrete must be taken into account in determining their gross income for the relevant tax year. Congress's creation of a special rule for "the case of a trade or business" belies any suggestion that Section 6501(e)(1)(A) was intended to codify the *Uptegrove Lumber* approach across the board.

2. The Court in Colony *construed the pre-1954 version of the statute without addressing the post-1954 version*

Because the 1954 amendments were not made applicable to prior tax years, the Court in *Colony* granted certiorari to determine "whether assessments by the Commissioner of two asserted tax deficiencies" were barred by the three-year assessment period "provided in the Internal Revenue Code of 1939." 357 U.S. at 29. The taxpayer in *Colony* "had understated the gross profits on the sales of certain lots of land * * * as a result of having overstated the 'basis' of such lots by erroneously including in their cost certain unallowable items of development expense." *Id.* at 30. The IRS therefore assessed deficiencies for the 1946 and 1947 tax years, and it did so more than three but less than five years after the taxpayer had filed its return. *Ibid.* The Tax Court held that the deficiencies were timely because the taxpayer's overstatement of basis gave rise to an omission from gross income under Section 275(c), and the court of appeals affirmed. *Id.* at 31.

This Court reversed. Focusing on "the critical statutory language, 'omits from gross income an amount properly includible therein,'" the Court stated that it

was "inclined to think that the statute on its face lends itself more plausibly to the taxpayer's interpretation." *Colony*, 357 U.S. at 32-33. The Court observed, however, that "it cannot be said that the language is unambiguous," and it therefore "turn[ed] to the legislative history of [Section] 275(c)." *Id.* at 33. The Court found in that history "persuasive evidence" that the five-year assessment period applied only to cases involving "a taxpayer's omission to report some taxable item," and not to cases in which "the understatement of a tax arises from an error in reporting an item disclosed on the face of the return." *Id.* at 33, 36. The Court therefore agreed with the taxpayer that "the statute is limited to situations in which specific receipts or accruals of income items are *left out* of the computation of gross income." *Id.* at 33.

Although the Court in *Colony* observed that its holding was "in harmony with the unambiguous language of [Section] 6501(e)(1)(A) of the Internal Revenue Code of 1954," the Court declined to resolve "the speculative debate between the parties as to whether Congress [in the 1954 amendments] manifested an intention to clarify or change the 1939 Code." 357 U.S. at 37. The Court's failure to address the post-1954 version of the statute was "no mere oversight," since the parties in *Colony* had vigorously debated whose interpretation of the statute Congress had endorsed in the 1954 amendments. *Intermountain*, 650 F.3d at 702; see Pet. Br. at 23-24, *Colony*, *supra* (No. 306), 1958 WL 91875; Gov't Br. at 23–24, *Colony*, *supra* (No. 306), 1958 WL 91876; Pet. Reply Br. at 6–8, *Colony*, *supra* (No. 306), 1958 WL 91877. The Court did not resolve that debate and instead limited its holding to Section 275(c) of the 1939 Code. See *Colony*, 357 U.S. at 37.

3. Colony *does not control the interpretation of current Section 6501(e)(1)(A)*

Although the words "omits from gross income an amount properly includible therein" continue to appear in current Section 6501(e)(1)(A), the meaning of those words is now clarified by adjacent provisions of Section 6501(e) that were not part of the statutory scheme before the Court in *Colony*. Section 6501(e)(1)(A)(i), which contains a special definition of "gross income" that applies "[i]n the case of a trade or business," would be largely superfluous under petitioners' understanding of the basic rule set forth in Section 6501(e)(1)(A). See pp. 21-22, *supra*. And Section 6501(e)(2), by specifically referring to omissions of "items" that ought to have been included on an estate- or gift-tax return, indicates that the term "amount" in Section 6501(e)(1)(A) should not be equated with "item." See p. 23, *supra*. Congress's use of different terms in adjacent provisions indicates that *Colony*'s interpretation of Section 6501(e)(1)(A)'s predecessor, which the Court viewed as "limited to situations in which specific receipts or accruals of income items are *left out* of the computation of gross income," 357 U.S. at 33, would not be a sound interpretation of current law. See *Intermountain*, 650 F.3d at 704.

The Court in *Colony*, of course, had no need to consider the effect of the 1954 amendments. The Court was construing the statute as it existed before those amendments, and it did not discuss the implications of current Sections 6501(e)(1)(A)(i) and 6501(e)(2) for the interpretation of the extended-assessment-period provision. Consideration of the larger statutory context, however, is essential to a proper understanding of current Section 6501(e)(1)(A). See, *e.g.*, *United States* v. *Tinklenberg*, 131 S. Ct. 2007, 2012 (2011) ("[T]erms must be read in

their statutory context in order to determine how the provision in question should be applied in an individual case."); *Morton*, 467 U.S. at 828 ("We do not * * * construe statutory phrases in isolation; we read statutes as a whole."). Because the Court in *Colony* did not (and had no occasion to) perform that contextual analysis, its decision is not controlling here.

4. In any event, the Treasury regulation resolves the statutory ambiguity that Colony *identified*

a. Although the Court in *Colony* was "inclined to think that the statute on its face lends itself more plausibly to the taxpayer's interpretation," it acknowledged that "it cannot be said that the language is unambiguous." 357 U.S. at 33. Because the *Colony* Court recognized that an ambiguity existed, its construction of the words "omits from gross income an amount properly includible therein" did not preclude the Treasury Department from adopting, through a published regulation issued after notice-and-comment rulemaking, a different interpretation of the disputed statutory language. See *Brand X*, 545 U.S. at 983; see also *Mayo*, 131 S. Ct. at 711. "Only a judicial precedent holding that the statute unambiguously forecloses the agency's interpretation, and therefore contains no gap for the agency to fill, displaces a conflicting agency construction." *Brand X*, 545 U.S. at 982-983.

Under *Brand X*, the new Treasury Department regulation would be entitled to *Chevron* deference even if that rule construed precisely the same statutory provision that was before the Court in *Colony*. See *Brand X*, 545 U.S. at 982-983. But in fact, the regulation and the *Colony* decision address different statutory provisions (current Section 6501(e)(1)(A) and Section 275(c) of the

1939 Internal Revenue Code, respectively), albeit provisions that contain significant language in common. The Treasury Department's authority to act as it did is particularly clear because the agency, in adopting the new regulation, could consider the implications of adjacent statutory provisions that the *Colony* Court had no occasion to address.

b. Respondents place weight (Br. in Opp. 16) on the Court's observation in *Colony* that its conclusion was "in harmony with the unambiguous language of [Section] 6501(e)(1)(A) of the Internal Revenue Code of 1954." 357 U.S. at 37. Respondents view that statement as indicating that the Court's decision in *Colony* applies equally to the identical language contained in the 1939 and 1954 Codes. But given the Court's earlier recognition that the phrase "omits from gross income an amount properly includible therein" was ambiguous, see *id.* at 33 ("[I]t cannot be said that the language is unambiguous."), the Court's later reference to new Section 6501(e)(1)(A) cannot reasonably be understood to refer to the same language. That reading depends on the unlikely premise that "within the span of just four pages of the U.S. Reports," the Court (in an opinion by Justice Harlan) "illogically described essentially identical text as both ambiguous and unambiguous." *Intermountain*, 650 F.3d at 703.

The Court's reference to the "unambiguous language of [Section] 6501(e)(1)(A)" is far more sensibly read as describing the then-new subparagraph (i) in that provision, which for trades or businesses defines the term "gross income" to mean total receipts from sales of goods or services, without any offset for the trade or business's basis. See *Intermountain*, 650 F.3d at 697. Under that provision, an overstatement of basis in goods

or services sold by a trade or business like Colony could not trigger the six-year assessment period because such an overstatement would not affect the calculation of "gross income" as defined in Section 6501(e)(1)(A)(i). For that reason, the Court's disposition of *Colony* was apparently "in harmony with" the outcome that Section 6501(e)(1)(A)(i) would have mandated. 357 U.S. at 37. But that analysis does not apply to respondents, who did not operate a trade or business, and whose overstatement of basis therefore resulted in an understatement of "gross income."

Respondents argue (Br. in Opp. 17-18) that *Colony*'s result cannot have been in harmony with recently-added subparagraph (i), because *Colony* involved the sale of land rather than goods or services. It is correct that land is normally not considered a good. See, *e.g.*, Gov't Br. at 45-46, *Salman Ranch I*, *supra* (No. 2008-5053), 2008 WL 4133498. The taxpayer at issue in *Colony*, however, was a real estate developer that was subdividing farm land into residential lots and selling those lots to individual buyers. See Pet. Br. at 3-4, *Colony*, *supra* (No. 306), 1958 WL 91875. *Colony* thus confronted the circumstance in which real property was the taxpayer-business's inventory rather than merely one of its assets. On its tax returns, the taxpayer in *Colony* reported its sales of land in the way that a business typically reports sales of goods or services. See *ibid.* The taxpayer also argued in the Tax Court that its overstatement of basis did not trigger the extended assessment period because its "omission resulted from an overstatement of *cost of goods sold*, rather than from an omission of gross receipts." *Colony, Inc.* v. *Commissioner*, 26 T.C. 30, 49 (T.C. 1956) (emphasis added). Thus, while an argument could be made that the phrase "sale of

goods or services" in subparagraph (i) does not encompass sales of land, the Court had sound reason to conclude that its disposition of *Colony* would have been no different under the amended statute.[8]

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

DONALD B. VERRILLI, JR.
Solicitor General
TAMARA W. ASHFORD
Deputy Assistant Attorney General
MALCOLM L. STEWART
Deputy Solicitor General
JEFFREY B. WALL
Assistant to the Solicitor General
GILBERT S. ROTHENBERG
MICHAEL J. HAUNGS
JOAN I. OPPENHEIMER
Attorneys

NOVEMBER 2011

---

[8] In addition, all but one of the cases that had arisen in the lower courts involved trades or businesses engaged in the sale of goods or services. See, *e.g.*, *Goodenow* v. *Commissioner*, 238 F.2d 20, 20-21 (8th Cir. 1956); *Davis* v. *Hightower*, 230 F.2d 549, 550-551 (5th Cir. 1956); *Deakman-Wells Co.* v. *Commissioner*, 213 F.2d 894, 895 (3d Cir. 1954); *Uptegrove Lumber Co.*, 204 F.2d at 571; but see *Slaff* v. *Commissioner*, 220 F.2d 65, 66 (9th Cir. 1955). It would therefore have been reasonable for the Court to conclude that the 1954 amendments had settled the question not only in *Colony* but in virtually all other similar cases.

RESPONDENT'S BRIEF

RECORD AND BRIEFS

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA,
Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,
Respondents.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

BRIEF FOR RESPONDENTS

RICHARD T. RICE
Counsel of Record
C. MARK WILEY
MICHAEL R. CASHIN
ROBERT T. NUMBERS II
WOMBLE CARLYLE
SANDRIDGE & RICE LLP
One West Fourth Street
Winston-Salem, NC 27101
(336) 721-3600
rrice@wcsr.com

GREGORY G. GARRE
J. SCOTT BALLENGER
LORI ALVINO MCGILL
LATHAM & WATKINS LLP
555 11th Street, NW
Suite 1000
Washington, DC 20004
(202) 637-2207
gregory.garre@lw.com

ROGER J. JONES
ANDREW R. ROBERSON
LATHAM & WATKINS LLP
233 South Wacker Drive
Suite 5800
Chicago, IL 60606
roger.jones@lw.com

Library of Congress
Law Library

QUESTION PRESENTED

Whether the Internal Revenue Service has validly overruled this Court's holding in *Colony, Inc. v. Commissioner*, 357 U.S. 28 (1958)—that an overstatement of the basis of sold property is not an "omission" from gross income—and retroactively reopened and extended the statute of limitations applicable to respondents' tax returns.

RULE 29.6 STATEMENT

Home Oil and Coal Company, Inc. is the only corporate respondent. There is no parent corporation or publicly held corporation that owns 10% or more of the stock of that company.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

RULE 29.6 STATEMENT ii

TABLE OF AUTHORITIES v

INTRODUCTION 1

STATEMENT OF THE CASE 4

A. Statutory History 4

B. Regulatory Background And Son-Of-BOSS 9

C. Facts Relevant To This Litigation 11

D. The New Treasury Regulations 14

E. Decisions Below 17

SUMMARY OF ARGUMENT 19

ARGUMENT 22

I. THE THREE-YEAR STATUTE OF LIMITATIONS APPLIES UNDER THE SETTLED LAW IN PLACE BEFORE THE RECENT TREASURY REGULATIONS 22

A. As This Court Held In *Colony*, An Overstatement Of Basis Is Not An "Omission" From Gross Income 22

B. The Government's Attempt To Sidestep And Rewrite *Colony* Is Unavailing 29

C. Congress Has Ratified This Court's Interpretation In *Colony* 33

Page

II. THE 2010 TREASURY REGULATION DOES NOT—AND CANNOT—COMPEL A DIFFERENT RESULT HERE 36

A. *Colony* Conclusively Resolved the Statutory Question Presented 36

B. By Its Own Terms, The Regulation Does Not Apply To The Tax Returns At Issue 39

C. In Any Event, The Regulation Is Invalid 45

1. If The Regulation Must Be Given Retroactive Effect, It Is *Ultra Vires* 45

2. The Regulation Is Not Entitled To *Chevron* Deference 48

3. The Regulation Is Procedurally Defective 50

III. THE COMMISSIONER HAS AMPLE TOOLS AT HIS DISPOSAL TO IDENTIFY AND TIMELY ADDRESS PERCEIVED TAX SHELTER TRANSACTIONS 51

CONCLUSION 54

TABLE OF AUTHORITIES

Page(s)

CASES

Auer v. Robbins,
519 U.S. 452 (1997) 44, 45

Automobile Club of Michigan v. Commissioner,
353 U.S. 180 (1957) 46

Bakersfield Energy Partners, LP v. Commissioner,
568 F.3d 767 (9th Cir. 2009) 11, 42

Beard v. Commissioner,
633 F.3d 616 (7th Cir. 2011) 42

Benderoff v. United States,
398 F.2d 132 (8th Cir. 1968) 33, 42

Bishop v. United States,
338 F. Supp. 1336 (N.D. Miss. 1970), *aff'd*,
1972 U.S. App. LEXIS 10892 (5th Cir. 1972) ... 33, 42

Boulware v. Commissioner,
552 U.S. 421 (2008) 10

Bowen v. Georgetown University Hospital,
488 U.S. 204 (1988) 20, 41, 45, 48

Burks v. United States,
633 F.3d 347 (5th Cir. 2011) 42, 47, 49

Page(s)

Carcieri v. Salazar,
555 U.S. 379 (2009) 41

Carr v. United States,
130 S. Ct. 2229 (2010) 40

CC&F Western Operations Ltd. Partnership v. Commissioner,
273 F.3d 402 (1st Cir. 2001) 42

Chenault v. United States Postal Service,
37 F.3d 535 (9th Cir. 1994) 44

Chevron U.S.A., Inc. v. NRDC, Inc.,
467 U.S. 837 (1984) 20, 37, 38

Chock Full O'Nuts Corp. v. United States,
453 F.2d 300 (2d Cir. 1971) 48

Colony, Inc. v. Commissioner,
26 T.C. 30 (1956) 6

Colony, Inc. v. Commissioner,
357 U.S. 28 (1958) ..... *passim*

Cullen v. Pinholster,
131 S. Ct. 1388 (2011) 40

Davis v. Hightower,
230 F.2d 549 (5th Cir. 1956) 5

Page(s)

In re Enterprise Mortgage Acceptance Co., Securities Litigation,
391 F.3d 401 (2d Cir. 2004) 44

FDA v. Brown & Williamson Tobacco Corp.,
529 U.S. 120 (2000) 38

Florida Department of Revenue v. Piccadilly Cafeterias, Inc.,
554 U.S. 33 (2008) 34

Forest Grove School District v. T.A.,
557 U.S. 230, 129 S. Ct. 2484 (2009) 34

General Dynamics Land Systems, Inc. v. Cline,
540 U.S. 581 (2004) 38

Gonzales v. Oregon,
546 U.S. 243 (2006) 45

Goodenow v. Commissioner,
238 F.2d 20 (8th Cir. 1956) 5

Hanover Bank v. Commissioner,
369 U.S. 672 (1962) 10

Hughes Aircraft Co. v. United States,
520 U.S. 939 (1997) 43

INS v. St. Cyr,
533 U.S. 289 (2001) 20, 44

Page(s)

Intermountain Insurance Service of Vail, LLC v. Commissioner,
134 T.C. 211 (2010), *rev'd*, 650 F.3d 691 (D.C. Cir. 2011) 16, 44

Intermountain Insurance Service of Vail, LLC v. Commissioner,
650 F.3d 691 (D.C. Cir. 2011) 25, 31

Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA,
130 S. Ct. 1605 (2010) 34

John R. Sand & Gravel Co. v. United States,
552 U.S. 130 (2008) 34

Ketcham v. Commissioner,
142 F.2d 996 (2d Cir. 1944) 5

Klamath Strategic Inv. Fund, LLC v. United States,
440 F. Supp. 2d 608 (E.D. Tex. 2006) 48

Landgraf v. USI Film Products,
511 U.S. 244 (1994) 44

Lazarus v. United States,
142 F. Supp. 897 (Ct. Cl. 1956) 5

Levy v. Sterling Holding Co.,
544 F.3d 493 (3d Cir. 2008), *cert. denied*, 129 S. Ct. 2827 (2009) 43

Page(s)

Lieberman v. Cambridge Partners, L.L.C.,
432 F.3d 482 (3d Cir. 2005) 44

Lorillard v. Pons,
434 U.S. 575 (1978) 34

Marbury v. Madison,
5 U.S. (1 Cranch) 137 (1803) 36

Mayo Foundation for Medical Education & Research v. United States,
131 S. Ct. 704 (2011) 48

Murfam Farms, LLC v. United States,
88 Fed. Cl. 516, 526 (2009) 48

Myers v. United States,
30 A.F.T.R.2d (RIA) 5332 (S.D. Cal. 1972) 33, 42

National Cable & Telecommunications Association v. Brand X Internet Services,
545 U.S. 967 (2005) 38, 39

Patterson v. McLean Credit Union,
491 U.S. 164 (1989) 34

Phinney v. Chambers,
392 F.2d 680 (5th Cir 1968) 42

Pope v. Shalala,
998 F.2d 473 (7th Cir. 1993), *overruled on other grounds by Johnson v. Apfel*, 189 F.3d 561 (7th Cir. 1999) 6, 43

Page(s)

Quaker State Oil Refining Corp. v. United States, 24 Cl. Ct. 64 (1991), *aff'd*, 994 F.2d 824 (Fed. Cir. 1993) 42

Quick Trust v. Commissioner, 54 T.C. 1336 (1970), *acq.*, 1970-2 C.B. xxi, *aff'd per curiam*, 444 F.2d 90 (8th Cir. 1971) 33

Ramaprakash v. FAA, 346 F.3d 1121 (D.C. Cir. 2003) 50

Reis v. Commissioner, 142 F.2d 900 (6th Cir. 1944) 5

Rhone-Poulenc Surfactants & Specialties, L.P. v. Commissioner, 114 T.C. 533 (2000) 42

Rock Island, Arkansas & Louisiana Railroad v. United States, 254 U.S. 141 (1920) 1

Russell F. Davis, Inc. v. United States, 170 F. Supp. 185 (N.D. Ind. 1959) 34, 42

Sala v. United States, 552 F. Supp. 2d 1167 (D. Colo. 2008) 48

Salman Ranch Ltd. v. United States, 573 F.3d 1362 (Fed. Cir. 2009) 11, 42

SEC v. Chenery Corp., 318 U.S. 80 (1943) 47

Page(s)

Slaff v. Commissioner,
220 F.2d 65 (9th Cir. 1955) 5

Smiley v. Citibank (South Dakota), N.A.,
517 U.S. 735 (1996) 41, 49

Stobie Creek Invs., LLC v. United States, 82
Fed. Cl. 636 (2008), *aff'd*, 608 F.3d 1366
(Fed. Cir. 2010) 48

Talk America, Inc. v. Michigan Bell Telephone Co.,
131 S. Ct. 2254 (2011) 45

Transpac Drilling Venture 1982-12 v. Commissioner,
147 F.3d 221 (2d Cir. 1998) 47

United States v. Morton,
467 U.S. 822 (1984) 49

University Country Club, Inc. v. Commissioner,
64 T.C. 460 (1975), *acq.*, 1976-2 C.B. 3 33

Uptegrove Lumber Co. v. Commissioner,
204 F.2d 570 (1953) 4, 5, 7, 31

W.C. & A.N. Miller Development Co. v. Commissioner,
81 T.C. 619 (1983) 32

Page(s)

White v. Commissioner,
991 F.2d 657 (10th Cir. 1993) 42

STATUTORY AND REGULATORY PROVISIONS

5 U.S.C. § 553 50
5 U.S.C. § 553(b)(B) 50

26 U.S.C. § 22(a) (1940) 23

26 U.S.C. § 61(a)(3) (2006) 23

26 U.S.C. §446 30

26 U.S.C. § 451 30

26 U.S.C. § 754 3

26 U.S.C. § 6011 52
26 U.S.C. § 6011(a) 51

26 U.S.C. § 6111 52

26 U.S.C. § 6112 52

26 U.S.C. § 6501 1
26 U.S.C. § 6501(e)(1)(A) 1, 30

26 U.S.C. § 6707 52

26 U.S.C. § 6707A 52

Page(s)

26 U.S.C. § 6708 52

26 U.S.C. § 7602(a) 51

26 U.S.C. § 7805(b)(3) 47

26 U.S.C. § 7805 (note) 46

Act of Jan. 6, 1954, ch. 736, 68A Stat. 3 ..... 5, 6

Pub. L. No. 73-216, 48 Stat. 680 (1934)
(reenacted in 53 Stat. 87 (1939)) 4

Pub. L. No. 89-44, 79 Stat. 136 (1965) 8, 9

Pub. L. No. 91-172, 83 Stat. 487 (1969) 9

Pub. L. No. 91-614, 84 Stat. 1836 (1970) 9

Pub. L. No. 94-455, 90 Stat. 1520 (1976) 9

Pub. L. No. 97-248, 96 Stat. 324 (1982) 8

Pub. L. No. 99-514, 100 Stat. 2085 (1986) 8

Pub. L. No. 104-168, 110 Stat. 1452 (1996) 46

Pub. L. No. 108-357, 118 Stat. 1418 (2004) 9, 10, 11, 27

Pub. L. No. 111-147, 124 Stat. 71 (2010) 9, 16

T.D. 6172, 1956-1 C.B. 565 (1956) 9

Page(s)

T.D. 9466, 2009-43 I.R.B. 551 (Sept. 24, 2009), *reprinted in* 74 Fed. Reg. 49,321 (Sept. 28, 2009) 14, 15

T.D. 9511, 2011-1 C.B. 455 (Dec. 15, 2010), *reprinted in* 75 Fed. Reg. 78,897 (Dec. 17, 2010) 16, 17, 40, 41

Temp. Treas. Reg. § 1.6011-4T, *reprinted in* 67 Fed. Reg. 64,799 (Oct. 22, 2002) 52

Temp. Treas. Reg. § 301.6501(e)-1(T)(b) 15

Treas. Reg. § 29.22(a)-5 (1943) 6

Treas. Reg. § 301.6501(e)-1(e) (2010) 3, 17, 39

OTHER AUTHORITIES

Black's Law Dictionary (9th ed. 2009) 47

Benjamin J. Cohen & Catherine A. Harrington, *Is the Internal Revenue Service Bound by Its Own Regulations and Rulings?*, 51 Tax Law. 675 (1998) 46

CCN-2010-001 (Nov. 23, 2009), *available at* http://www.irs.gov/pub/irs-ccdm/cc-2010-001.pdf 15

Page(s)

Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack Of) Compliance With Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727 (2007) 50

H.R. Rep. No. 104-506 (1996).....46

Internal Revenue Manual (Mar. 12, 2010), *available at* http://www.irs.gov/irm/part1/irm_01-015-002.html 47

IRS Gen. Couns. Mem. 36856 (Sept. 21, 1976) 9

John F. Manning, *Constitutional Structure and Judicial Deference to Agency Interpretations of Agency Rules*, 96 Colum. L. Rev. 612 (1996).....45

William S. McKee et al., *Federal Taxation of Partnerships and Partners* (2005) 27

Non-Docketed Service Advice Review 11419, 2000 WL 34423427 (July 10, 2000) 9

Notice 2000-44, 2000-2 C.B. 255 10

Staff of the Joint Comm. on Taxation, Summary of Conference Agreement on H.R. 3838 (Tax Reform Act of 1986) (Comm. Print 1986) 8

INTRODUCTION

As every taxpayer knows, "[m]en must turn square corners when they deal with the Government." *Rock Island, Ark. & La. R.R. v. United States*, 254 U.S. 141, 143 (1920). If a taxpayer missed a deadline for requesting a refund from the Internal Revenue Service (IRS) under the applicable limitations period as interpreted by this Court, that would be the end of the matter. The ultimate question in this case is whether the rule of law runs both ways. In particular, the question is whether (or in what circumstances) the IRS may reopen and extend the time within which it must act under a statute of limitations, even when doing so would require the IRS retroactively to reject this Court's own interpretation of the statute.

The Internal Revenue Code requires the IRS to assess additional taxes within three years of the date a tax return is filed, unless a statutory exception applies. 26 U.S.C. § 6501. Three years is the default rule that applies in the vast majority of cases; it gives the IRS and its countless agents ample time to review a return and decide whether to audit it. The limitations period is extended to six years if the taxpayer "omits from gross income an amount properly includable therein" constituting more than 25% of the taxpayer's gross income on the return. *Id.* § 6501(e)(1)(A). Here, it is undisputed that the IRS missed the three-year deadline. The IRS argues, however, that the six-year limitations period applies, because respondents purportedly "omit[ted] from gross income" a triggering amount by overstating their basis in sold property.

This Court resolved the meaning of "omits from gross income" in this exact statutory context more than 50 years ago. The Court held that an

overstatement of basis does *not* result in an "omi[ssion]" from gross income, and that Congress gave the IRS an extra three years only when the taxpayer "fail[s] to report particular income receipts and accruals," and not "whenever gross income was understated." *Colony, Inc. v. Comm'r*, 357 U.S. 28, 35 (1958). *Colony* was the law, as understood by Congress, the courts, and the IRS for decades—until the IRS fell behind a few years ago in auditing taxpayers that had engaged in a type of partnership transaction that the IRS now believes lacked "economic substance." At that point, after losing in court on its argument that the statute does not mean what this Court held it does, the IRS took the extraordinary step of seeking retroactively to extend the statute of limitations by adopting the very interpretation that this Court rejected in *Colony*.

In defending that remarkable administrative action, the government pursues three basic strategies:

(1) It recycles the same arguments that this Court considered, and rejected, in *Colony* as to the meaning of statutory language that has not changed in any material way despite numerous amendments to, and reenactment of, the provision at issue;

(2) It suggests that certain 1954 amendments—which left the key "omits from gross income" language untouched—transform the meaning of that language, even though the *Colony* Court observed that the amended version of the statute was "in harmony with" its statutory holding; and

(3) It argues that a regulation issued in late 2010, which was designed to reverse the IRS's recent losses in court, effectively displaces *Colony* and

requires that the statutory language be given an entirely different meaning—retrospectively.

None of those arguments is persuasive. *Colony* conclusively resolved the meaning of the key statutory language and, indeed, concluded that Congress had "address[ed] itself to the specific situation" at issue here. 357 U.S. at 33. To the extent these issues were debatable then, they are now settled by *stare decisis* bolstered by congressional reenactment of the relevant language without change in 1986. The government's case therefore boils down to the recent Treasury regulation—and the IRS's own effort to *change* the law. That regulation by its terms applies only "to taxable years with respect to which the period for assessing tax *was open on or after September 24, 2009*." Treas. Reg. § 301.6501(e)-1(e) (2010) (emphasis added). The limitations period at issue here was not "open on or after September 24, 2009," because the three-year limitations period had expired in April 2003—at which time the law was this Court's decision in *Colony*. Even if the regulation could be read to apply retroactively, it is invalid. The IRS lacks the power retroactively to overrule a decision of this Court conclusively interpreting a statute in order to control the outcome of litigation to which the government is a party.

The government spills considerable ink about the allegedly abusive nature of the underlying transactions. The IRS has more than ample tools—and agents—at its disposal to identify and address such concerns. Here, the basis step-up about which the government complains was the subject of a valid election by respondents under 26 U.S.C. § 754—fully disclosed and apparent on the face of the partnership return. Moreover, the Court's resolution of the

statutory question presented will affect *all* taxpayers—including those who have engaged in transactions the IRS recognizes are legitimate—and a broad range of issues that have nothing to do with so-called "Son-of-BOSS" transactions. In addition, the startling theory of administrative law—and accountability—on which the government's brief rests has far-reaching implications beyond the tax context.

As Judge Wilkinson observed below, while agencies have unquestioned leeway to act within the bounds set by Congress and the courts, "it remains the case that agencies are not a law unto themselves." Pet. App. 20a (concurring). "No less than any other organ of government, they operate in a system in which the last words in law belong to the Congress and the Supreme Court." *Id.* The administrative action at issue here transgresses the bounds of any reasonable application of that bedrock constitutional principle. The judgment of the court of appeals should be affirmed.

STATEMENT OF THE CASE

A. Statutory History

1. In 1934, Congress enacted former-§ 275(c), which extended the three-year limitations period within which the IRS was generally required to assess income taxes to five years where "the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return." Pub. L. No. 73-216, § 275(c), 48 Stat. 680, 745 (1934) (reenacted in 53 Stat. 87 (1939)).

Litigation ensued over the proper scope of § 275(c). In *Uptegrove Lumber Co. v. Commissioner*—which involved a manufacturing company that included an

inflated cost item in its calculation of the cost of goods sold—the Third Circuit held that § 275(c) applies where a taxpayer fails "to include some receipt or accrual in his computation of gross income and not in a more general way to errors of whatever kind in that computation." 204 F.2d 570, 572 (1953). *Uptegrove* was followed by three other courts of appeals and the Court of Claims. *See Slaff v. Comm'r*, 220 F.2d 65 (9th Cir. 1955); *Davis v. Hightower*, 230 F.2d 549 (5th Cir. 1956); *Goodenow v. Comm'r*, 238 F.2d 20 (8th Cir. 1956); *Lazarus v. United States*, 142 F. Supp. 897 (Ct. Cl. 1956). The Sixth Circuit, by contrast, adopted the government's contrary interpretation of § 275(c). *See, e.g., Reis v. Comm'r*, 142 F.2d 900 (6th Cir. 1944).

The lower courts also divided over whether former-§ 275(c) applied when a taxpayer failed to include some income receipt or accrual in gross income but nevertheless *disclosed* that item somewhere else on the face of the return. *See, e.g., Slaff*, 220 F.2d at 66-67; *Uptegrove*, 204 F.2d at 573. *But see Ketcham v. Comm'r*, 142 F.2d 996, 997 (2d Cir. 1944).

2. In 1954, Congress revised and reenacted the Internal Revenue Code. Act of Jan. 6, 1954, ch. 736, 68A Stat. 3. As part of that revision, former-§ 275(c) was re-codified as § 6501(e)(1)(A) and titled "General rule." The key "omits from gross income" language was carried over unchanged. Congress also added two new subparagraphs to § 6501(e)(1)(A).

Subparagraph (i) provided that, "[i]n the case of a trade or business, the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services ... prior to diminution by the cost of such sales or services." 68A Stat. at 804 (§ 6501(e)(1)(A)(i)). That definition clarified the proper

computation rules that apply in the context of the sale of goods or services by certain businesses, like the manufacturing company in *Uptegrove*, for determining whether any actual omission exceeds the 25% threshold for the extended limitations period—in a way that *favored* taxpayers. Under Treasury regulations then in effect and considered by the *Uptegrove* court, the cost of goods sold and other items had been subtracted from gross receipts in the case of a trade or business to arrive at gross income. *See Uptegrove*, 204 F.2d at 571 (citing Treas. Reg. § 29.22(a)-5 (1943)).

Subparagraph (ii) clarified existing law and provided that items adequately disclosed on the return or in a statement attached thereto also shall not count in calculating "the amount omitted from gross income." 68A Stat. at 805 (§ 6501(e)(1)(A)(ii)).

3. A few years after the 1954 amendments, this Court granted certiorari in *Colony* to resolve the question whether an understatement of gross income resulting from an overstatement of basis in sold property constitutes an "'omi[ssion] from gross income [of] an amount properly includible therein'" under the former-§ 275(c). 357 U.S. at 30. The Court held, in an opinion authored by Justice Harlan, that an overstatement of basis is *not* an omission from gross income. *Id.* at 31-37. *Colony* was decided after the 1954 amendments, but on the basis of former-§ 275(c).

The taxpayer in *Colony* was a developer that subdivided and sold real property to individual buyers. 357 U.S. at 30. The taxpayer's federal income tax returns reported the amount realized from the sales of individual lots, subtracted the cost of the lots (*i.e.*, its basis in the property), and arrived at a figure for its net gain. *Id.*; *Colony, Inc. v. Comm'r*, 26 T.C. 30, 38-39

(1956). In calculating its basis in the lots, the taxpayer "erroneously includ[ed] in their cost certain unallowable items of development expense." 357 U.S. at 30. Because the taxpayer's basis was overstated, the return understated the gain from the transactions. *Id.*

Examining the "critical statutory language," this Court explained that the plain and ordinary meaning of "omit" is "'[t]o leave out or unmentioned; not to insert, include, or name,'" *id.* at 32, and observed that the government's interpretation would replace "omits" with "understates," *id.* at 35. The Court also considered the legislative history, which revealed Congress's "purpose ... to give the Commissioner an additional two years to investigate tax returns in cases where, because of a taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors." *Id.* at 36. The Court concluded that "Congress was addressing itself to the specific situation where a taxpayer actually omitted some income receipt or accrual in his computation of gross income, and not more generally to errors in that computation arising from other causes." *Id.* at 33.

The Court further observed that the Commissioner's interpretation "not only would ... read § 275(c) more broadly than is justified by the evident reason for its enactment," but would also "create a patent incongruity in the tax law," because it would treat errors related to overstated amounts affecting "gross income" (*e.g.*, basis or cost of goods sold) differently than "overstated deductions," though the amount of both types of errors are shown on the return and could have an equal impact on tax owed. *Id.* at 36-37 (citing *Uptegrove*, 204 F.2d at 573). Although the case was decided based on former-§ 275(c), the parties

brought the 1954 amendments to the Court's attention. The Court observed that its interpretation of § 275(c) was "in harmony with the unambiguous language" of § 275(c)'s successor, § 6501(e)(1)(A). *Id.* at 37.

4. In 1965, seven years after *Colony*, Congress changed the heading of § 6501(e) from "Omission from Gross Income" to "Substantial Omission of Items," and added § 6501(e)(3), relating to excise taxes. Pub. L. No. 89-44, § 810(b), 79 Stat. 136, 169 (1965). Congress did not change the key phrase "omits from gross income an amount properly includible therein."

In 1982, Congress enacted the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), Pub. L. No. 97-248, 96 Stat. 324, 648, which created a single, unified procedure for determining the tax treatment of all partnership items at the partnership level. TEFRA added § 6229(c)(2), which contains language substantively identical to that of former-§ 275(c) at issue in *Colony*, but applies only to partnerships. Section 6229(c)(2) does not contain the language that appears in subparagraphs (i)-(ii) of § 6501(e)(1)(A).

In 1986, Congress re-enacted the Internal Revenue Code as revised, retaining the phrase "omits from gross income" without change. *See* Tax Reform Act of 1986, Pub. L. No. 99-514, § 2, 100 Stat. 2085, 2095; *see also* Staff of the Joint Comm. on Taxation, Summary of Conference Agreement on HR 3838 (Tax Reform Act of 1986) 79 (Comm. Print 1986) (explaining that the law "reenacts the provisions of the 1954 Code—as in effect on the date of the enactment of the bill—together with amendments made by the conference agreement").

All told, since *Colony*, the critical statutory language interpreted in *Colony* has remained

untouched, through a total of six substantive amendments to § 6501(e) and the 1986 reenactment.[1]

B. Regulatory Background And Son-Of-BOSS

In January 1956, after the 1954 amendments and before this Court's decision in *Colony*, the Commissioner issued final regulations under § 6501(e)(1)(A) that simply tracked the text of the statute as amended. *See* T.D. 6172, 1956-1 C.B. 565. Those regulations remained unchanged until 2009, when the regulations at issue here were issued in temporary and proposed form. *See infra* at 14-15.

For decades following *Colony*, the IRS recognized and followed *Colony* without question. In 1976, the IRS recognized *Colony* as "[t]he landmark" case construing § 6501(e), while acknowledging that *Colony*'s holding is "in harmony with" § 6501(e)(1)(A). IRS Gen. Couns. Mem. 36856 (Sept. 21, 1976). As late as July 2000—three months *after* the returns at issue here were filed—the Commissioner reiterated his view that "the extended statute of limitations provided in the case of a 25% omission is limited to when *specific receipts or accruals are left out* of the computation of gross income." Non-Docketed Service Advice Review (NSAR) 11419, 2000 WL 34423427 (July 10, 2000) (emphasis added). That view changed abruptly in the 2000s, not because of any epiphany concerning the meaning of § 6501(e), but because of the advent of a

---

[1] Pub. L. No. 89-44, § 810(a), (b), 79 Stat. 136, 169 (1965); Pub. L. No. 91-172, § 101(g)(3), 83 Stat. 487, 525 (1969); Pub. L. No. 91-614, § 102(d)(8), 84 Stat. 1836, 1842 (1970); Pub. L. No. 94-455, § 1307(d)(2)(F)(vi), 90 Stat. 1520, 1728 (1976); Pub. L. No. 108-357, § 413(c)(28), 118 Stat. 1418, 1509 (2004); Pub. L. No. 111-147, § 513(a), 124 Stat. 71, 111 (2010).

transaction called "Son-of-BOSS" and the IRS's failure to timely review returns reporting such transactions.[2]

In August 2000, four months after respondents' returns were filed, the IRS issued Notice 2000-44, 2000-2 C.B. 255 (published Sept. 5, 2000), which set forth, in some detail, the IRS's position that tax consequences claimed by taxpayers in connection with certain partnership transactions (generally referred to as "Son-of-BOSS" transactions) were contrary to the spirit of the Code. The IRS does not deny that a literal application of the Code's partnership-basis provisions produces the result that taxpayers claim, but it contends—and several courts have held—that the Code's language can be disregarded in these circumstances under the judicially-created "economic substance" doctrine. *See* U.S. Br. 3-4. In the ensuing months and years, the IRS took several steps to identify and educate its examiners about transactions fitting the Son-of-BOSS pattern. *See infra* at 52-53.

In 2004, Congress amended § 6501 by adding a new subsection (c)(10), which provides that, in the case of a "listed" transaction like "Son-of-BOSS," the limitations period for assessing tax does not expire until one year after the taxpayer submits certain information. American Jobs Creation Act of 2004 (AJCA), Pub. L. No. 108-357, § 814(a), 118 Stat. 1418. If the taxpayer fails to furnish the required information, the limitations period remains open indefinitely. Section 6501(c)(10) is

---

[2] General Counsel Memoranda and NSARs are internal guidance for IRS personnel issued by the IRS's National Office. Like private letter rulings, they are not binding on the government, but are evidence of the IRS's views and practice. *Hanover Bank v. Comm'r*, 369 U.S. 672, 686-87 (1962); *see also Boulware v. Comm'r*, 552 U.S. 421, 431 (2008) (citing NSAR).

not retroactive, and the IRS does not contend that it applies to the returns at issue here.[3]

Meanwhile, the IRS began an aggressive program of asserting tax deficiencies related to Son-of-BOSS and similar transactions, even when the three-year limitations period had expired. The IRS began to argue, for the first time in the more than 50 years since this Court decided *Colony*—and contrary to the guidance the IRS had issued since *Colony*—that this Court's holding in *Colony* applies only in the context of the sale of goods or services by a trade or business and not to a taxpayer's basis in property. The Tax Court promptly rejected that statutory argument, and the Ninth Circuit affirmed. *Bakersfield Energy Partners, LP v. Comm'r*, 568 F.3d 767, 778 (9th Cir. 2009). The Federal Circuit agreed. *Salman Ranch Ltd. v. United States*, 573 F.3d 1362, 1372 (Fed. Cir. 2009).

C. Facts Relevant To This Litigation

Respondents, small business owners in Salisbury, North Carolina, unwittingly became swept up in this chain of events when they decided in 1999 to sell a small co-family business called Home Oil & Coal Company, Inc. (Home Oil). JA 24. Home Oil had been in operation for more than 50 years before the transactions at issue in this case. JA 114-19. Respondents Robert Pierce and Stephen Chandler became the principal owners and day-to-day managers of Home Oil in 1985. *Id.* Over the years, Home Oil

---

[3] Section 6501(c)(10) is effective for tax years with respect to which the period for assessing a deficiency "did not expire" before October 22, 2004. 118 Stat. at 1581.

changed the focus of its business from heating oil and coal to concrete and building supplies. JA 115-16.

By 1999, Pierce and Chandler were the only two shareholders of Home Oil. JA 118-19. Pierce, who owned approximately 81% of the outstanding shares, decided to retire and sell the business. Pet. App. 2a. Given the importance of the sale for himself and his family, Pierce—a small business owner who was far from expert in such matters—sought financial planning assistance from several highly recommended financial and legal professionals. *Id.*; JA 24-25. On advice from those professionals, the following transactions occurred prior to the sale of the business:

(1) Home Concrete & Supply, LLC was formed on April 15, 1999. Home Concrete's initial members were Pierce, Chandler, Home Oil, and two trusts for the benefit of Pierce's children (collectively, the "partners").

(2) On May 13, 1999, each partner commenced a short sale of Treasury notes.

(3) On May 17, 1999, each partner contributed the proceeds from the short sales of Treasury notes, together with the short Treasury note positions and margin cash, to Home Concrete as capital contributions.

(4) On May 18, 1999, Home Concrete closed its Treasury note short positions by purchasing Treasury notes in the open market.

(5) On June 11, 1999, Home Oil transferred substantially all of its business assets to Home Concrete as a capital contribution.

(6) On June 14, 1999, each partner transferred a percentage of its membership interests in Home Concrete to Home Oil as a capital contribution to Home Oil.

(7) In connection with such transfers, Home Concrete made an election pursuant to 26 U.S.C. § 754 to step up the basis of its assets.

(8) On August 31, 1999, Home Concrete sold substantially all of its assets to a third party for a gross sales price of $10,623,348.

See JA 25-29.[9]

Home Concrete timely filed its partnership tax return on or before April 17, 2000. JA 29, 124. That return reported the sale of Home Concrete's assets, including the gross sales price ($10,623,348), the partnership's original basis ($4,542,824.36), the election to adjust its basis, and the resulting stepped-up basis ($10,527,350.53). JA 143, 150, 151. Home Concrete also attached Form 8594 (Asset Acquisition Statement Under Section 1060), on which it reported the third-party purchaser's information and the fair market value of the sold assets. JA 143.

The partners also filed their respective federal income tax returns for the 1999 tax year on or before April 17, 2000. JA 29, 30, 152, 189, 217, 274, 288. Each

---

[9] The government repeatedly (and erroneously) refers to the "sale of Home Concrete" and "the partnership's sale price" instead of the sale of the *assets* of the partnership. The distinction is significant. By selling *property*—here capital assets—Home Concrete was required to (and did) complete Form 4797, Sales of Business Property, and, among other things, describe the specific property sold, its sale price, the cost or basis of the property, and the resulting gain or loss. JA 139-42.

partner reported his, her, or its portion of the gain from the sale of the partnership's assets on the relevant return. JA 179, 198, 233, 281, 295. Each partner that had engaged in short sale transactions further disclosed that "during the year the proceeds of a short sale not closed by the taxpayer during this tax year were received." JA 204, 258.

Despite its public pronouncement in Notice 2000-44, and notwithstanding respondents' substantial disclosures, the IRS and its agents inexplicably waited nearly *six years* to even begin auditing Home Concrete's 1999 return. In a letter dated February 23, 2006, the IRS notified Pierce that Home Concrete's return had "been selected for examination" because of a "Notice 2000-44 Transaction." Add. 19a-21a. Six months later, on September 7, 2006, the IRS issued a Notice of Final Partnership Administrative Adjustment (FPAA), in which the IRS asserted that respondents' claimed basis in the sale of Home Concrete's assets was too high. JA 95-97. The IRS has never alleged that the 1999 returns were fraudulent.

D. The New Treasury Regulations

In September 2009, after the government had lost several Son-of-BOSS cases on statute of limitations grounds and was still litigating others (including this case), the Department of the Treasury withdrew its longstanding regulations tracking the text of § 6501 and issued new temporary regulations under §§ 6501 and 6229, purporting to limit the statutory language at issue in *Colony* to situations involving the sale of goods or services by a trade or business. *See* T.D. 9466, 2009-43 I.R.B. 551 (Sept. 24, 2009), *reprinted in* 74 Fed. Reg. 49,321 (Sept. 28, 2009). As relevant here, Temp. Treas. Reg. § 301.6501(e)-1T(a)(1)(iii) defined gross income—

outside the sale of goods or services in a trade or business—as "the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property." "Consequently," the regulation asserted, "an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A)." 74 Fed. Reg. at 49,323. In a provision titled "Effective/applicability date," Treasury provided that the new regulation would "apply to taxable years with respect to which the applicable period for assessing tax did not expire before September 24, 2009." *Id.* (Temp. Treas. Reg. § 301.6501(e)-1T(b)).

The temporary regulations were issued without any notice-and-comment period. Instead, the government simultaneously issued temporary and proposed regulations with identical text and requested comments within 90 days. 74 Fed. Reg. at 49,354. During this 90-day comment period, the IRS issued a Chief Counsel Notice purporting to interpret the "effective date" provision to mean that the regulations are applicable when the limitations period, *as interpreted in the regulations*, remains "open." CCN-2010-001 (Nov. 23, 2009), *available at* http://www.irs.gov/pub/irs-ccdm/cc-2010-001.pdf.

The government began arguing in ongoing litigation that the temporary regulations were an "intervening 'change in the law'" applicable to pending cases in which the three-year statute of limitations undeniably had closed under this Court's interpretation in *Colony*. The *en banc* Tax Court unanimously rejected the government's reliance on the regulations, holding that the regulations, by their terms, do not apply to tax

years that had closed under the statute as interpreted by *Colony*, and that in any event the regulations are invalid and not entitled to deference. *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 134 T.C. 211, 224-25 (2010) (denying government's motion to vacate and reconsider), *rev'd*, 650 F.3d 691 (D.C. Cir. 2011).[4]

In December 2010, the government withdrew the temporary regulations and issued virtually identical final regulations. T.D. 9511, 2011-1 C.B. 455 (Dec. 15, 2010), *reprinted in* 75 Fed. Reg. 78,897 (Dec. 17, 2010).[5]

---

[4] Two concurring judges concluded that the temporary regulations were invalid for failing to comply with the APA's notice-and-comment requirements. 134 T.C. at 243-44.

[5] Although it is nearly identical to the temporary regulation, the final regulation introduces an inconsistency that underscores the arbitrary nature of the IRS's action. After the temporary regulation was issued, but before the final regulation was promulgated, Congress amended § 6501(e)(1), reorganizing a portion of § 6501(e)(1)(A), and once again leaving intact the phrase "omits from gross income." *See* Hiring Incentives to Restore Employment Act of 2010, Pub. L. No. 111-147, § 513, 124 Stat. 111. Although the temporary regulation cites § 6501(e)(1)(A) (which contains the general rule concerning "omits from gross income"), *see* Temp. Treas. Reg. § 301.6501(e)-1(a)(1)(iii), the final regulation states that "an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A)(i)." 75 Fed. Reg. at 78,899. The reference to § 6501(e)(1)(A)(i) in the final rule thus creates an anomaly. If it was intended to be a reference to the pre-March 2010 version of the statute (which applies in this case), it would make no sense. In that version, § 6501(e)(1)(A)(i) is the subparagraph that applies to the sale of goods or services by a trade or business. So the final regulation would purport to make overstatements of the cost of goods sold in a trade or business an "omission" from gross income—directly contradicting the government's interpretation of subparagraph (i) as well as subparagraph (a)(1)(ii) of the

The final regulations state that they "appl[y] to taxable years with respect to which the period for assessing tax *was open* on or after September 24, 2009." Treas. Reg. § 301.6501(e)-1(e) (emphasis added). The preamble to the regulations asserts that the regulations "are not retroactive" because they "do not reopen closed tax years." 75 Fed. Reg. at 78,898.

E. Decisions Below

In December 2006, respondents filed suit in district court, alleging that their tax-reporting positions were correct and that, in any event, the IRS was barred by the three-year limitations periods in §§ 6501(a) and 6229(a) from assessing any tax for the 1999 tax year. *See* JA 9. On cross-motions, the district court granted partial summary judgment to the government. Although the court agreed "that the language of § 275(c)" interpreted by this Court in *Colony* "is virtually identical" to § 6501(e)(1)(A), it held that the addition of subparagraph (i) changed what "omits from gross income" means in cases *not* involving the sale of goods or services by a trade or business. Pet. App. 34a.

The Fourth Circuit reversed. It concluded that this Court "in *Colony* straightforwardly construed the phrase 'omits from gross income,' unhinged from any dependency on the taxpayer's identity as a trade or

---

regulation. If, on the other hand, the IRS meant to reference the statute as amended in 2010, it refers to the provision specifying the computational 25% threshold—and would make the regulations purely *prospective*, because the March 2010 amendment by its terms does not apply to this case. *See supra* at n.3. Either way, the reference to § 6501(e)(1)(A)(i) in the final regulation demonstrates the hastiness with which the IRS acted in promulgating the final regulations and underscores the arbitrary nature of its rule.

business selling goods or services." *Id.* at 10a. Rejecting the government's attempt to "press[] another path around *Colony*" by way of its new regulation, the court explained that: (1) the regulation does not apply by its plain terms, because the period for assessing tax for the 1999 tax year was not "open" on September 24, 2009; (2) *Chevron* deference is not warranted because *Colony* had found Congress's intent on the specific issue was clear; and (3) the regulation could not in any event be applied retroactively to this case, because it would "change the law governing the taxpayer's 1999 returns and thereby subject them to liability to which they would not have been subject under pre-regulation law." *Id.* at 12a-16a.

Although the court of appeals did not need to reach respondents' alternative argument that the taxpayers adequately disclosed the amounts on their returns for purposes of § 6501(e)(1)(A)(ii), the court noted that Home Concrete "reported the basic components of the transactions"; "the taxpayers' individual" returns disclosed that the short sales were "not closed" during 1999; the partnership return included its "§ 754 election form [which] gave, for each partnership asset, an itemized accounting of the partnership's inside basis, the amount of the basis adjustment, and the post-election basis"; and the return "[o]n its face" also showed the sale of the Treasury Bonds with the cost, sales price, and resulting gain. *Id.* at 4a.

Judge Wilkinson joined the court's opinion in full but wrote separately to elaborate on why *Colony* is best viewed as a "*Chevron* step one" decision, and why

the agency's new interpretation is not entitled to any deference. *See id.* at 18a-19a (concurring).[6]

SUMMARY OF ARGUMENT

The statutory question presented should sound familiar to this Court. More than 50 years ago, the Court held that an overstatement of basis does *not* result in an "omi[ssion]" from gross income, and that Congress intended to give the IRS extra time for making tax assessments under the statute of limitations at issue here only when the taxpayer "fail[s] to report particular income receipts and accruals"—not "whenever gross income [i]s understated." *Colony*, 357 U.S. at 35. Principles of *stare decisis* coupled with congressional reenactment of the same language foreclose the government's amnesic attempt to relitigate the same statutory question today as if it reaches the Court on a blank slate. For decades following *Colony*, Congress, the courts, and the IRS all understood that this Court's interpretation of the key language at issue governed. Under that settled interpretation, the statute of limitations for respondents' tax returns expired in April 2003.

The government's case therefore comes down to the regulation issued by Treasury in 2010—while this case was on appeal—in an effort to overrule this Court's statutory interpretation in *Colony* after a string of losses in the lower courts on the meaning of the

---

6 The government has abandoned any reliance in this case on § 6229(c)(2), which governs a partnership's tax returns. *See supra* at 8; U.S. Sur-Reply at 14 (E.D.N.C. Apr. 19, 2007) (ECF No. 21). As explained by *amicus curiae* Bausch & Lomb Inc., however, the problems with the government's position in this case are only magnified when it comes to § 6229(c)(2).

statutory language at issue. While the IRS's power is indeed broad, the agency has yet to reach the point—if it ever could in our constitutional system—where it can override the settled decisions of this Court and retroactively reopen and extend a closed limitations period for the purpose of taking penal action against taxpayers. For several reasons, the government's attempt to achieve that result here should be rejected.

By its own terms, the regulation applies only "to taxable years with respect to which the period for assessing tax *was open on or after September 24, 2009*." The limitations period for respondents' returns was *not* "open on or after September 24, 2009," because the three-year limitations period expired in April 2003 under the law in effect at that time (*i.e.*, this Court's decision in *Colony*). At best, the regulation sends conflicting signals on whether it applies retroactively, and that alone is fatal to the agency's argument that the regulation reaches back to the returns at issue. A law that is ambiguous concerning its retroactive effect is "unambiguously *prospective*." *INS v. St. Cyr*, 533 U.S. 289, 320 n.45 (2001) (emphasis added); *see Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 208 (1988). No measure of agency deference can change that.

If the regulation applied by its terms to the returns at issue, it would be invalid. This Court's decision in *Colony* left no ambiguity for the IRS to "interpret." Although it seems artificial to try to view *Colony* through the lens of *Chevron U.S.A., Inc. v. NRDC, Inc.*, 467 U.S. 837 (1984), Justice Harlan wrote with great prescience and clarity for the Court in explaining—in language that closely tracks the *Chevron* step one test—that Congress "*address[ed] itself to the specific situation* where a taxpayer actually

omitted some income receipt or accrual in his computation of gross income, and not more generally to errors in that computation arising from other causes." *Colony*, 357 U.S. at 33 (emphasis added). Especially given Congress's reenactment of the key statutory language after *Colony*, there is no gap for the agency to fill, much less any basis to adopt the very interpretation that this Court rejected in *Colony*.

Furthermore, the IRS lacks the power, as a matter of statutory and constitutional law, retroactively to overrule a decision of this Court conclusively interpreting a statute. Congress has authorized the IRS to promulgate retroactive rules for *certain* purposes, but it has not authorized the kind of extraordinary retroactive rule at issue in this case. And even if the agency had such authority, the regulation at issue here would not be entitled to deference because it was set in stone before any opportunity for notice and comment, blatantly seeks to reverse the Commissioner's losses in pending litigation to which the agency was a party, and—for the reasons stated by this Court in *Colony*—is not a reasonable interpretation of the statute.

The IRS, like all agencies, enjoys deference within its proper areas of expertise. But as Judge Wilkinson observed below, the agency action at issue in this case "pass[es] the point where the beneficial application of agency expertise gives way to a lack of accountability and risk of arbitrariness." Pet. App. 20a (concurring).

ARGUMENT

I. THE THREE-YEAR STATUTE OF LIMITATIONS APPLIES UNDER THE SETTLED LAW IN PLACE BEFORE THE RECENT TREASURY REGULATIONS

In April 2000, when respondents filed their returns for the 1999 tax year, the law was settled that an overstatement of basis does not constitute an "omi[ssion] from gross income" within the meaning of § 6501(e)(1)(A). This Court so held in *Colony*, interpreting identical statutory language, and the IRS had accepted that reading of *Colony* for decades. The government now recycles the same statutory arguments that it advanced—and this Court rejected—in *Colony*, even though the "critical statutory language" that was the subject of this Court's holding has been reenacted by Congress in the decades since *Colony*. 357 U.S. at 32. The government also argues that the addition of a subparagraph in the 1954 amendments impliedly eviscerated *Colony*'s unqualified holding, even though this Court in *Colony* was well aware of the addition and stated that its holding was "in harmony with" § 6501(e)(1)(A). *Id.* at 37. The government's arguments should be rejected.

A. As This Court Held In *Colony*, An Overstatement Of Basis Is Not An "Omission" From Gross Income

1. In *Colony*, Congress's selection of the word "omits" instead of "reduces or understates"—combined with other indicia of Congress's intent—led this Court to conclude that "Congress was addressing itself to the specific situation where a taxpayer actually omitted some income receipt or accrual in his computation of

gross income, and not more generally to errors in that computation arising from other causes." *Id.* at 33. That interpretation was correct.

As even the government acknowledges, the plain and ordinary meaning of the verb "omit" is "to leave out" or "to fail to include or mention." *See* U.S. Br. 18-19 (and authorities cited therein); *Colony*, 357 U.S. at 32-33; Pet. App. 18a (Wilkinson, J., concurring). A taxpayer thus does not "omit" gross income where he includes every sales price or gross receipt but overstates his basis. As this Court explained in *Colony*, the legislative history unmistakably confirms that Congress intended that reading. 357 U.S. at 33-35. The government nevertheless proceeds in this case as if this Court's interpretation in *Colony* has no more force than a taxpayer's reading of the Code, simply repeating the same arguments that this Court considered and rejected in *Colony*. Those arguments are no more persuasive now than they were in 1958.

a. Just as it did in *Colony*, the government relies principally on the Code's definition of "gross income." *See* Brief for U.S., *Colony*, 357 U.S. 28 (1958) (No. 306), 1958 WL 91876, at *15-16 (U.S. *Colony* Br.). Then, as now, the definition of "gross income" expressly included "gains ... derived from ... dealings in property." 26 U.S.C. § 22(a) (1940); 26 U.S.C. § 61(a)(3) (2006). Then, as now, the government argued that an overstatement of basis was an omission from gross income, because the term "gross income" includes gain from the sale of property. *Colony* squarely rejected that argument. This Court acknowledged that "where a cost item is overstated ... gross income is affected to the same degree as when a gross-receipt item of the same amount is completely omitted from a tax return."

357 U.S. at 32. The Court, however, held that this interpretation fails to take account of "the word 'omits,' which Congress selected when it could have chosen another verb such as 'reduces' or 'understates,' either of which would have pointed significantly in the Commissioner's direction." *Id.*

b. The government also argues that § 6501(e)(1)(A) "must be interpreted in light of Congress's reasons for extending the assessment period involving omissions from gross income," which (the government says) was that "substantial omissions from gross income ... are often difficult to detect." U.S. Br. 24. It contends that basis overstatements are hard to discover—like omissions of income items, but "[u]nlike (for example) a potentially improper deduction, which provides a natural trigger for IRS inquiry." *Id.* Once again, this Court rejected precisely this argument in *Colony*.

Colony involved a basis overstatement. This Court squarely rejected the government's premise that such errors are more analogous to omissions of income items than to "overstated deductions." 357 U.S. at 36. The Court explained that the extended limitations period was intended for circumstances "where, because of a taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors." *Id.* at 36. "In such instances the return on its face provides no clue to the existence of the omitted item." *Id.* In contrast, "when, *as here*, the understatement of a tax arises from an error in reporting an item disclosed on the face of the return"—as opposed to the omission of "some taxable item" altogether—"the Commissioner is at no such disadvantage." *Id.* (emphasis added). In fact, the Court concluded that the government's interpretation

would introduce a "patent incongruity" into the tax law that Congress could not have intended, by treating overstated basis differently than overstated *deductions*, *id.*—which the IRS correctly concedes cannot constitute an omission from gross income. A deduction, like basis, appears as an amount on the face of a return. An overstated deduction is no less "difficult to detect" than an overstated basis.

The government now asks the Court not only to resurrect that very same "patent incongruity," but to adopt a new one. The government argues that an understatement of gross income attributable to an overstatement *of the cost of goods sold in a trade or business* would be subject to the three-year limitations period, while sales of *other property* in the same context could be subject to the six-year limitations period. That reading is untenable.

Colony involved a taxpayer engaged in the sale of *real property*, so it would make no sense to conclude that *Colony*'s interpretation of the key statutory language was limited to overstatement *of the cost of goods sold*. And although Congress clarified in the 1954 amendments how to calculate *gross income* concerning the sale of goods or services in "the case of a trade or business," § 6501(e)(1)(A)(i), in doing so it did not touch the general rule established by § 6501(e)(1)(A)—and confirmed by *Colony*—that an overstatement of basis does not result in an *omission* from gross income (however calculated).[7]

---

[7] One court has remarked that the taxpayer in *Colony* "described itself as a taxpayer in a trade or business with income from the sale of goods or services." *Intermountain Ins. Serv. of Vail, LLC v. Commissioner*, 650 F.3d 691, 703 (D.C. Cir. 2011). That is incorrect. This Court's decision recognizes that the

Moreover, reporting sales of property (involving "basis") requires more detailed disclosures than sales involving cost of goods sold—including specific descriptions of the property, acquisition date, sale date, sale price, cost basis (including adjustments for depreciation, improvements, and sale expenses), and gain or loss. Because the extended limitations period was intended to apply when the IRS "is at a special disadvantage in detecting errors," *Colony*, 357 U.S. at 36, it would be nonsensical for Congress to grant the IRS six years in a "basis" case while limiting the IRS's time to three years for a "cost of goods sold" case.[8]

c. The government tries to bolster this already-rejected argument by using the tax returns here as an example, and asserting that those returns did not give the IRS any fair chance to detect the alleged deficiency. U.S. Br. 25. Far from supporting its position, the returns simply confirm the conclusions this Court reached in *Colony*. Respondents' returns gave the IRS far more than a "clue" as to the legal dispute that ultimately developed:

(1) Home Concrete's return is marked "initial return" on its first page, showing that the partnership was created in 1999. JA 124.

---

underlying transaction concerned the sale of *real property*, 357 U.S. at 30, as did the parties' briefs in the case, *see* Br. for Petr., *Colony*, 357 U.S. 28 (1958) (No. 306), 1958 WL 91875, at *3 (Petr. *Colony* Br.); U.S. *Colony* Br. 4.

[8] The government repeatedly conflates two distinct concepts: "basis"—at issue in *Colony*—and "cost of goods sold"—at issue in cases like *Uptegrove*. "Basis" is the cost of property (*e.g.*, a capital asset), and is determined on an asset-by-asset basis. "Cost of goods sold" is used to account for the costs of inventory when it is sold, and is determined in the aggregate.

(2) The Form 8594 attached to the Home Concrete return clearly shows a sale of the partnership's assets as well as the total sales price of $10,623,348. JA 143-44.

(3) There was a substantial elective basis adjustment shown on the § 754 election schedule conspicuously attached to the Home Concrete return. JA 150, 151. The returns here disclosed an election that increased Home Concrete's basis in its assets by *more than 150%*.[9]

(4) Schedule D to the Home Concrete return shows that it reported the sale of U.S. Treasury Bonds with proceeds of $7,472,405, a notably large transaction outside the scope of what might be

---

[9] The IRS has understood for decades that § 754 elections (or non-elections) may operate to shift, defer, or eliminate tax liability in problematic ways. When partnership interests are transferred, § 754 permits, but does not require, the partnership to adjust its "inside" basis in its assets to match the partners' "outside" basis. Congress adopted that election in 1954 to address practical problems created by the prior rules, which had required that inside basis be adjusted according to fair market value (and therefore often required an appraisal of partnership assets). The potential for tax-shifting or avoidance was well-understood at the time, and has been continuously studied since. *E.g.*, William S. McKee et al., *Federal Taxation of Partnerships and Partners* ¶ 24.11[8] (2005) ("The wisdom of making basis adjustments elective has been debated since the election first appeared in 1954."). Congress has chosen to impose limitations but not eliminate the election entirely, because the realistic alternatives present even greater problems. For example, Congress amended the law in 2004 to *require* the election when a partnership has a substantial built-in loss, to minimize the extent to which existing tax losses can be shifted from outgoing to incoming partners. Pub. L. No. 108-357 § 833(b).

expected from a relatively small concrete company. JA 128.

(5) The Home Concrete return shows over $21 million in revenue—$3.7 million from gross receipts (JA 124), $10.6 million from the sale of assets (JA 143), and $7.4 million from the sale of Treasury notes (JA 128)—yet only a minimal taxable gain, because of the basis increase produced by the § 754 election.

(6) The Home Concrete return shows $8,693,414 in distributions to its partners. JA 126. This is a large amount to distribute in the first year of a partnership's existence.

(7) The individual partners attached statements to their respective returns disclosing that:

> **"DURING THE YEAR THE PROCEEDS OF A SHORT SALE NOT CLOSED BY THE TAXPAYER DURING THIS TAX YEAR WERE RECEIVED."**

JA 204, 258 (emphasis in original).[10]

---

[10] Home Concrete realized a short-term capital gain of $113,362 as a result of the short sales. JA 28. This gain was reported by Home Concrete on Schedule D, line 1(f). JA 128. There was nothing "misleading" about this disclosure. U.S. Br. 17. Under the category for short-term capital gains and losses recognized on assets held for one year or less, Schedule D provides a column for "Date acquired" and another column for "Date sold," under which the corresponding dates should be listed with regard to a particular short-term capital asset. JA 128. The individual partners opened the short sales, which are disclosed on their respective returns, on May 13, 1999. JA 26, 204, 258. Home Concrete purchased Treasury bonds to close the short sales on May 18, which is indicated in the "Date acquired" column on

The fact that the IRS did not examine the returns until long after the three-year period expired had nothing to do with the disclosures, or lack thereof, on the returns. The IRS simply failed to examine respondents' returns for nearly six years. Congress reserved the extended statute of limitations in § 6501(e)(1)(A) for situations where the "omission to report some taxable item" puts the IRS "at a special disadvantage in detecting errors." *Colony*, 357 U.S. at 36. It was not designed to help the IRS where, as here, the agency's failure to detect the alleged error is due to its own failure to timely act on disclosed facts.

B. The Government's Attempt To Sidestep And Rewrite *Colony* Is Unavailing

The government argues that a subparagraph added in the 1954 amendments somehow renders *Colony*'s interpretation of "omits from gross income" defunct or limits *Colony*'s holding to the sale of goods or services by a trade or business. Neither of these arguments is persuasive. Congress amended former-§ 275(c) in several respects in 1954. In every instance, the change favored taxpayers and limited the application of the six-year statute of limitations to situations in which the Commissioner truly was at a special disadvantage to detect errors. Congress did not make the broad brush change in the trigger for the six-year statute of limitations that the government hypothesizes—*to the detriment of taxpayers*. More fundamentally, the

---

Schedule D. JA 27, 128. Home Concrete then used the Treasury Bonds to close the short sales that had been opened by the individual partners, which is indicated in the "Date sold" column on Schedule D. JA 128. Respondents' returns thus reflect the short sale accurately, just as required by the IRS's own forms.

government's effort to side-step *Colony* based on the 1954 amendments is fatally undermined by the fact that this Court in *Colony* observed that its interpretation of the critical language was "in harmony with" the 1954 amendments. 357 U.S. at 37.

a. The government's argument that subparagraph (i) changes the meaning of "omits from gross income" is refuted by the statute's terms and structure. Section 6501(e)(1)(A)—which includes the "omits from gross income language—is entitled "General rule." The government describes subparagraphs (i) and (ii) as "*exceptions* to the general rule." U.S. Br. 20 (emphasis added). Congress, however, which knows well how to delineate "exceptions," did no such thing here. *Compare, e.g.*, 26 U.S.C. § 446 (stating "[e]xceptions" to a "[g]eneral rule"); *id.* § 451 (listing "[g]eneral rule" and then "[s]pecial rule[s]" addressed to particular situations). Moreover, subparagraph (i) does not even address the crucial "omits from gross income" language interpreted in *Colony*. It simply defines what "gross income" means for particular sales "in the case of a trade or business." *Id.* § 6501(e)(1)(A)(i).

b. There is no credible basis for the government's assertion that "[t]he principal effect of subparagraph (i) is to eliminate the possibility that a trade or business could trigger the six-year assessment period by overstating its basis in sold property." U.S. Br. 21. Subparagraph (i) applies only to sales of "goods or services," not "property" generally. Although the subparagraph is consistent with the result reached in pre-*Colony* cases involving the sale of goods or services by a trade or business like *Uptegrove*, it also settled that a Treasury regulation (discussed in *Uptegrove*) defining gross income in the context of the

sale of goods by certain businesses did not apply for the computational purpose of determining when an actual "omission" triggered the 25% threshold. *See Uptegrove*, 204 F.2d at 571; Add. 18a. In any event, there is no basis to read subparagraph (i)'s explication of what qualifies as "gross income" in a particular context as an effort to rewrite what constitutes an "*omission* from gross income" in all others.[11]

It is not unusual for Congress to spell out the application of a general rule to a specific fact pattern, even if there would be a belts-and-suspenders component to its action. But it would be unusual, if not unprecedented, for Congress to nullify a general rule that it leaves unchanged simply by adding a subsection addressing a specific fact pattern. And it would be even more unheard of for Congress to do so without leaving behind in the text, legislative history, or otherwise any meaningful evidence that it intended to achieve that counter-intuitive result.

c. The government now contends that the inferences it wants to draw are necessary to give the

---

[11] In *Intermountain*, the court of appeals concluded that "Congress intended subsection (i) to resolve that debate [in the lower courts over former-§ 275(c)] in the taxpayer's favor, *though only in the trade or business context*." 650 F.3d at 704 (emphasis added). There is no evidence, however, that subparagraph (i) was designed to change the general rule in a way that *disfavored* taxpayers in all other contexts. What we *do* know is that this Court concluded that its decision in *Colony*—a case involving the sale of real property, not the sale of goods and services by a trade or business—was "in harmony with" the 1954 amendments. 357 U.S. at 37. The Court could not have reached that conclusion if it viewed subparagraph (i) as *changing* what constitutes an "omission from gross income" for taxpayers other than a trade or business involved in the sale of goods or services.

amendment "'real and substantial effect,'" because the computational function concededly served by subparagraph (i) supposedly is "irrelevant to the issue that had spawned a circuit split" before *Colony*. U.S. Br. 22-23. The government's argument (at 21) that subparagraph (i) created a "special rule" rests on the mistaken premise that the definition of "gross income" is determinative of whether there has been an "omi[ssion]" from gross income—an argument that was considered and rejected in *Colony*. Because subparagraph (i) concededly is *not* rendered superfluous under the taxpayer's interpretation, U.S. Br. 22, there is no reason to adopt the bizarre theory proposed by the government: that Congress intended *sub silentio* to change the "General rule" in former-§ 275(c) that it left untouched by adding a subparagraph addressing only a particular situation.

d. Finally, *Colony* cannot be limited in the way the government contends because *Colony* involved the sale of real property, which the government correctly acknowledges is neither a "good" nor a "service." U.S. Br. 52. Nor is it "inventory," as the government now contends, under well-established case law and the IRS's long-standing position. *See W.C. & A.N. Miller Dev. Co. v. Comm'r*, 81 T.C. 619, 628 & n.5 (1983) (citing 1921 IRS published ruling and 1928 Board of Tax Appeals opinion). Because subparagraph (i) would not have applied on the facts of *Colony*, it is inconceivable that this Court's statement that its interpretation of § 275(c) was "in harmony with" § 6501(e)(1)(A) embraced the government's reading of the subparagraph—which would wipe out *Colony*.

The government states (at 49) that "[t]he Court in *Colony*, of course, had no need to consider the effect of

the 1954 amendments." In *Colony*, however, both parties relied on the 1954 amendments. *See* Petr. *Colony* Br. 23-24; U.S. *Colony* Br. 23-24. The Solicitor General specifically argued that the 1954 amendments "confirm[ed]" that "the courts below correctly held that § 275(c) was applicable to the case at bar." U.S. *Colony* Br. at 24. In reaching the opposite conclusion, the Court in *Colony* necessarily rejected that argument.[12]

C. Congress Has Ratified This Court's Interpretation In *Colony*

1. The 1954 amendments were not designed to address this Court's decision in *Colony* because they were enacted several years before *Colony* was decided. If Congress had disagreed with *Colony*—or *Colony*'s statement that the Court's decision was "in harmony with" the 1954 amendments—Congress had decades to act. Not only has Congress never acted to overrule this Court's interpretation in *Colony*, it has repeatedly amended the provision at issue—and affirmatively reenacted it in 1986—leaving the operative language unchanged. *See supra* at 8-9.

When Congress reenacted § 6501 as part of the 1986 Code, it did so against the backdrop of *Colony* and cases applying *Colony*'s holding to the 1954 Code.[13]

---

[12] The government notes (at 46-47) that the Senate and House Reports accompanying the 1954 amendments refer to "changes in existing law." Those reports simply list all the changes to the language of subsection (e); they by no means suggest that the law was changed in the way the government contends.

[13] *See, e.g., Benderoff v. United States*, 398 F.2d 132, 137 (8th Cir. 1968); *Univ. Country Club, Inc. v. Comm'r*, 64 T.C. 460, 469 (1975); *Quick Trust v. Comm'r*, 54 T.C. 1336, 1347 (1970), *aff'd per curiam*, 444 F.2d 90 (8th Cir. 1971); *Myers v. United States*, 30

Such congressional ratification, coupled with principles of *stare decisis*, resolves any doubt as to the continuing vitality and controlling force of *Colony*. *See Forest Grove Sch. Dist. v. T.A.*, 557 U.S. 230, 129 S. Ct. 2484, 2492 (2009); *Lorillard v. Pons*, 434 U.S. 575, 580 (1978). Indeed, as this Court has stated, "[c]onsiderations of *stare decisis* have special force in the area of statutory interpretation," because "Congress remains free to alter what [the Court] ha[s] done." *Patterson v. McLean Credit Union*, 491 U.S. 164, 172-73 (1989); *see also, e.g., John R. Sand & Gravel Co. v. United States*, 552 U.S. 130, 139 (2008) (quoting *Patterson*).

2. Congress also re-enacted the phrase "omits from gross income" when it created § 6229(c)(2) in 1982, which extends the limitations period to six years when a *partnership* "omits from gross income" an amount in excess of 25% of the *partnership*'s gross income. Congress is presumed to have adopted *Colony*'s interpretation of the language it reenacted. *See Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA*, 130 S. Ct. 1605, 1616 (2010). Congress did not include in § 6229(c)(2) the language in § 6501(e)(1)(A)(i) that the government argues limits *Colony*'s holding. Yet the Commissioner contends that § 6229(c)(2) should be given the same interpretation as § 6501(e)(1)(A). *See generally* Br. of Bausch & Lomb Inc. as *Amicus Curiae* Supporting Respondents. That position makes it all the more implausible for the government to ascribe any significance to subparagraph (i). The more significance the

---

A.F.T.R.2d (RIA) 5332 (S.D. Cal. 1972); *Bishop v. United States*, 338 F. Supp. 1336, 1352 (N.D. Miss. 1970), *aff'd*, 1972 U.S. App. LEXIS 10892 (5th Cir. 1972); *Russell F. Davis, Inc. v. United States*, 170 F. Supp. 185, 186 (N.D. Ind. 1959).

government tries to attach to subparagraph (i) now, the more significant it must be that Congress did not include that subparagraph in § 6229(c)(2).

3. Congress's post-*Colony* change in 1965 to the heading of § 6501—from "Omission from Gross Income" to "Substantial Omission of *Items*"—underscores that Congress understood and affirmatively endorsed the *Colony* holding. 79 Stat. at 169 (emphasis added). A subchapter heading is one of the "'tools available for the resolution of a doubt about the meaning of a statute.'" *Florida Dep't of Revenue v. Piccadilly Cafeterias, Inc.*, 554 U.S. 33, 47 (2008) (citation omitted). If Congress had intended the interpretation now advanced by the government, it hardly would have changed the heading in a way that fits naturally with this Court's decision in *Colony*—but directly contradicts the government's position that Congress did *not* have in mind the omission of "items."[14]

---

[14] The government's reliance (at 49) on § 6501(e)(2) is misplaced. Congress added paragraph (2) as part of the 1954 amendments, to cover estate and gift taxes. Unlike § 6501(e)(1)(A), (e)(2) specifically refers to the omission of "items" includible in the gross estate or total gifts. In the government's view, Congress's failure to change the word "amount" in § 6501(e)(1) (retained from former-§ 275(c)) to the new phrasing it used in § 6501(e)(2) lends support to its interpretation by negative implication. This Court in *Colony*, however, considered Congress's "use of the word 'amount' (instead of, for example, 'item')," and concluded that Congress intended to give the IRS more time only "where, because of a taxpayer's omission to report some taxable item, the Commission is at a special disadvantage in detecting errors." 357 U.S. at 36. The far more relevant point when it comes to Congress's use of "item" is Congress's change to the heading for § 6501(a)(1) in 1965, which must be viewed as an affirmative endorsement of this Court's statutory holding in *Colony*.

In short, even if *Colony* somehow could be read as having left the door open on the proper reading of the statutory language at issue, Congress's subsequent actions against the backdrop of *Colony* have closed it.

II. THE 2010 TREASURY REGULATION DOES NOT—AND CANNOT—COMPEL A DIFFERENT RESULT HERE

After two courts of appeals had rejected the IRS's argument that *Colony* does not foreclose the interpretation that the government advances here, the IRS sought to address the problem by wiping out *Colony*. So it issued a regulation adopting the very reading of the key "omits from gross income" language that this Court had rejected in *Colony*. The government promptly invoked that regulation on appeal in this case, in an effort to overcome the fundamental flaws in its statutory interpretation of § 6501(e)(1)(A). The new regulation cannot change the result here, for several independent reasons.

A. *Colony* Conclusively Resolved the Statutory Question Presented

This Court's decision in *Colony* definitively declared "what the law is" with respect to the key statutory question at issue. *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 177 (1803). The government emphasizes a statement near the outset of this Court's statutory analysis in *Colony* that "it cannot be said that the language is unambiguous." 357 U.S. at 33; *see* U.S. Br. 10, 13, 48, 51. It is true that the Court recognized a possible ambiguity in the text (when read in a vacuum) if "one touches lightly on the word 'omits' and bears down hard on the words 'gross income.'" 357 U.S. at 32. The government overlooks that the Court said that it

was "inclined to think that the statute on its face lends itself more plausibly to the taxpayer's interpretation." *Id.* In any event, the critical point—also overlooked by the government—is that the Court then consulted other tools of statutory interpretation, including the legislative history, and concluded that Congress *had* definitively answered the statutory question presented. *See id.* at 33-37. In other words, based on all available evidence, the Court concluded that Congress's intent was *un*ambiguous.

Justice Harlan wrote for the Court with considerable prescience, and clarity, in explaining the Court's statutory interpretation in *Colony*. Tracking language that this Court would adopt four decades later in *Chevron* for determining when Congress's intent resolved the matter, he explained that "Congress was *addressing itself to the specific situation* where a taxpayer actually omitted some income receipt or accrual in his computation of gross income, and not more generally to errors in that computation arising from other causes." *Id.* at 33 (emphasis added); *compare with Chevron*, 467 U.S. at 842-43 (When "Congress has *directly spoken to the precise question at issue*," that is the end of the matter and "the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.") (emphasis added). Applying the traditional tools of statutory construction, this Court in *Colony* concluded that Congress had "directly spoken to the precise question at issue," and had instructed that an "omission from gross income" occurred *only* where an item of gross income had been left out entirely.

This Court has relied upon legislative history in finding that Congress's intent is unambiguous. *See,*

e.g., *General Dynamics Land Sys., Inc. v. Cline*, 540 U.S. 581, 587-90 (2004); *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 133, 137 (2000). Even if this Court decided today that courts should not consult legislative history under *Chevron*'s first step, there is no basis for an agency to disregard a pre-*Chevron* decision of this Court declaring Congress's intent simply because the Court—consistent with existing modes of statutory interpretation—consulted the legislative history and found it "persuasive." 357 U.S. at 33. While legislative history may have fallen out of favor in some quarters since this Court decided *Colony*, principles of *stare decisis* do not lose their force simply because a particular tool of statutory construction is no longer *en vogue*. For purposes of *stare decisis*, the statutory holding must govern.

If it were appropriate or necessary to try to dissect *Colony* through a *Chevron* lens, therefore, Judge Wilkinson was correct that *Colony* is best characterized as a "step one" case. *See* Pet. App. 18a (Wilkinson, J., concurring); *see also Chevron*, 467 U.S. at 843 n.9 ("If a court, employing traditional tools of statutory construction, ascertains that Congress had an intention on the precise question at issue, that intention is the law and must be given effect."). There is thus no room for the agency to overrule *Colony* by "reinterpreting" the statute, because there is no gap for the agency to fill. For that reason alone, the government's reliance (at 50-51) on *National Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967 (2005), is misplaced. Congress's ratification of this

Court's interpretation removes any doubt that the agency is not free to adopt a different one.[15]

B. By Its Own Terms, The Regulation Does Not Apply To The Tax Returns At Issue

1. Even if there were a gap for the agency to fill with respect to the meaning of "omits from gross income," the recent Treasury regulation on which the government relies in this case does not apply. That regulation applies only "to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009." Treas. Reg. § 301.6501(e)-1(e). The plain language of the regulation directs attention to whether the limitations period "was open" in September 2009 and, in particular, whether the "period for assessing tax" "was open" at that time. As explained, the governing law as of September 24, 2009 was this Court's decision in *Colony*. *See supra* at 22-36. The ordinary three-year limitations period therefore applied—and had long-since expired under existing law. The period for assessing respondents' tax

---

[15] *Brand X* did not involve an agency's attempt to supplant a statutory holding of this Court. An agency's decision to override an interpretation of a circuit court is at least consistent with the non-acquiescence doctrine under which agencies may decide not to follow the law of a particular circuit. In the constitutional scheme, however, there is something different, and more "disrupt[ive]," about an agency seeking to override a decision of *this* Court. Pet. App. 21a (Wilkinson, J., concurring); *cf. Brand X*, 545 U.S. at 1003 (Stevens, J., concurring). Even assuming, *arguendo*, that the rule of *Brand X* may be extended to Supreme Court decisions, there would have to be no doubt that this Court actually intended to leave room for an agency to override the Court's decision. *Colony* is not susceptible to such an interpretation.

liability thus was not—in any sense—"open on or after September 24, 2009."

The government's contrary argument relies on language that appears in a preamble to the regulation, which asserts that a taxable year is "open" if it is the "subject of any case pending before any court of competent jurisdiction ... in which a decision had not become final." 75 Fed. Reg. at 78,898. That is dangerous nonsense. Of course, in some sense a *case* remains open until the exhaustion of all appeals. A *limitations period* that has expired prior to the institution of litigation, however, remains expired and does not become "open" again merely because a case was filed. Were it otherwise, the government could never lose on statute of limitations grounds, because it could always simply file an action after the limitations period has expired and then claim that the limitations period is "open" merely because of pending litigation.

The government says (at 34-35) that the regulation's applicability clause must be read in light of its "substantive provisions," and that in determining whether the period was "open," the Court must apply the Commissioner's new interpretation of "omits from gross income," under which the "period" would be six years, not three. The regulation does not ask whether the limitations period "*would have* been open" in September 2009; it asks whether it "*was* open" on that date, an inquiry that naturally calls for application of the existing law on that date. Tenses matter. *Cf. Cullen v. Pinholster*, 131 S. Ct. 1388, 1398 (2011) (relying on Congress's use of past tense); *Carr v. United States*, 130 S. Ct. 2229, 2237 (2010) (giving effect to Congress's consistent use of the present tense, and contrasting Congress's use of "the past-perfect tense

... when coverage of preenactment events is intended"); *Carcieri v. Salazar*, 555 U.S. 379, 382 (2009) (concluding that phrase "now under Federal jurisdiction" refers to tribes under federal jurisdiction at the time of the statute's enactment).

At a minimum, the regulation does not clearly mandate retroactive application. Indeed, the very same preamble on which the government relies also states that the regulations "are not retroactive." 75 Fed. Reg. at 78,898. The text of the regulation (including the preamble) can in no way be said to mandate the retroactive application of the rule. That is fatal to the government's argument. Just as Congress must speak clearly when it wants to legislate retroactively, "administrative rules will not be construed to have retroactive effect unless their language *requires* this result." *Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 208 (1988) (emphasis added).

2. Perhaps appreciating that the rule's own text is insufficient to make it retroactive, the government suggests that the regulations are not retroactive "in the relevant sense" because they merely "clarify" the law. *See* U.S. Br. 40; *see also* Opp. to Pet. for Cert. at 15 n.4, *Beard v. Comm'r* (No. 10-1553). That argument is unavailing. This Court in *Colony* had settled the meaning of "omits from gross income" as excluding overstatements of basis on the ground they did not constitute omissions. *Supra* at XX. *That* was the law when respondents filed their 1999 tax returns. Indeed, until the new Treasury regulation, it was the nearly uniform view of the courts that *Colony*'s holding

applied to § 6501(e)(1)(A).[16] The regulation did not "clarify" that law; it sought to completely revamp it.

As explained above, *Colony* conclusively resolved the statutory question presented. Even assuming the statute was susceptible to the agency's interpretation, the regulation nonetheless would have effected a substantive change in then-existing law. *See Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 744 n.3 (1996) (recognizing that an agency regulation changing a prior interpretation of a statute may constitute an impermissibly retroactive change in the law). This Court's statutory holding in *Colony* had been the law for more than 50 years and had been recognized by the IRS. *See supra* at 9. There was no confusion about the

---

16 *See Benderoff*, 398 F.2d at 137; *White v. Comm'r*, 991 F.2d 657, 661-62 (10th Cir. 1993); *Salman Ranch Ltd. v. United States*, 573 F.3d 1362 (Fed. Cir. 2009); *Bakersfield Energy Partners, LP v. Comm'r*, 568 F.3d 767, 776 (9th Cir. 2009); *see also Rhone-Poulenc Surfactants & Specialties, L.P. v. Comm'r*, 114 T.C. 533, 557 (2000); *Quaker State Oil Refining Corp. v. United States*, 24 Cl. Ct. 64 (1991), *aff'd*, 994 F.2d 824 (Fed. Cir. 1993); *Myers*, 30 A.F.T.R. 2d (RIA) 5332; *Bishop*, 338 F. Supp. at 1352; *Russell F. Davis, Inc.*, 170 F. Supp. at 186. *But see Beard v. Comm'r*, 633 F.3d 616, 620 (7th Cir. 2011). *CC&F Western Operations Ltd. Partnership v. Commissioner*, cited by the government (at 41), is not to the contrary. That case did not involve a basis overstatement, was decided more than a year after respondents filed their returns, and merely questioned in dicta whether *Colony*'s interpretation carried over to § 6501. 273 F.3d 402 (1st Cir. 2001). The government relied below on the Fifth Circuit's decision in *Phinney v. Chambers*, 392 F.2d 680 (5th Cir 1968), for the proposition that *Colony*'s holding is limited to the sale of goods or services by a trade or business. *See* U.S. Br. (4th Cir. Apr. 30, 2010) at 12-13, 19, 26, 28-33, 35, 49, 58, 66-67, 75, 81. As that court has explained, however, *Phinney* did not so hold. *See Burks v. United States*, 633 F.3d 347, 352-53 (5th Cir. 2011); *id.* at 353 n.5.

statutory question presented after *Colony*—until the IRS issued the regulation at issue.

For those reasons (and others), the lower court decisions relied upon by the government (at 40-41) in arguing that the change at issue is merely a "clarification" are readily distinguishable. Those cases are nevertheless pertinent in one important respect: they recognize that "an enacting body's description of an amendment as a 'clarification'" is by no means controlling. *Levy v. Sterling Holding Co.*, 544 F.3d 493, 507 (3d Cir. 2008), *cert. denied*, 129 S. Ct. 2827 (2009) (citation omitted). Otherwise, "an agency could make a substantive change merely by referring to a new interpretation as a 'clarification.'" *Pope v. Shalala*, 998 F.2d 473, 483 (7th Cir. 1993), *overruled on other grounds by Johnson v. Apfel*, 189 F.3d 561 (7th Cir. 1999). That is precisely what the IRS attempts here.

The government also contends (at 41–42) that there is no "relevant" retroactivity problem here because the application of an enlarged statute of limitations is a mere "procedural rule[]," and "the regulation does not bear on the legality of petitioners' primary conduct." The government is mistaken. This Court has recognized that "extending a statute of limitations after the pre-existing period of limitations has expired impermissibly revives a moribund cause of action." *Hughes Aircraft Co. v. United States*, 520 U.S. 939, 950 (1997). Application of the new regulation to the returns at issue here would have a retroactive effect of the most direct and disfavored kind; it would "'attach[] a new disability, in respect to transactions ... already past'" by "impermissibly reviv[ing]" the IRS's cause of action and eviscerating an affirmative defense that respondents previously possessed. *Hughes*, 520 U.S. at

947-48, 950 (quoting *Landgraf v. USI Film Prods.*, 511 U.S. 244, 269 (1994)).[17]

3. The government's resort (at 31-32) to *Auer v. Robbins*, 519 U.S. 452, 461 (1997), cannot bridge this gap. U.S. Br. 31-32. First, as with a statute, a regulation that is "ambiguous with respect to retroactive application" must be construed "to be unambiguously prospective." *St. Cyr*, 533 U.S. at 320 n.45. There is "no ambiguity in such a [rule] for an agency to resolve." *Id.* Administrative deference principles cannot change that result. *See id.* (refusing to defer to agency interpretation of statute that was "ambiguous with respect to retroactive application").

Second, the Commissioner's interpretation exceeds the bounds of any conceivable deference. The government's interpretation is flatly inconsistent with the plain text of the regulation and any reasonable meaning of the phrase "was open." *Auer*, 519 U.S. at 461. The Tax Court has aptly called the government's position "irreparably marred by circular, result-driven logic and wishful notion that the ... regulations should apply to this case because [the taxpayer] was involved in what [the government] believes was an abusive transaction." *Intermountain Ins. Serv. of Vail, LLC v. CIR*, 134 T.C. 211, 219 (2010) (*en banc*), *rev'd*, 650 F.3d 691 (D.C. Cir. 2011). No measure of agency deference can sustain an interpretation of a rule that conflicts with the rule's own text and creates such a result.

---

[17] The harsh retroactive effect of extending a limitations period to resurrect time-barred actions has been widely acknowledged. *See, e.g., Lieberman v. Cambridge Partners, L.L.C.*, 432 F.3d 482, 489 (3d Cir. 2005); *In re Enter. Mortgage Acceptance Co., Sec. Litig.*, 391 F.3d 401, 406-07, 410 (2d Cir. 2004); *Chenault v. United States Postal Serv.*, 37 F.3d 535, 539 (9th Cir. 1994).

Third, the rationales for *Auer* deference are strained beyond the breaking point in these circumstances. The government is a party here—and issued both temporary and proposed final regulations simultaneously, without notice and comment—so there is "reason to suspect that the interpretation does not reflect the agency's fair and considered judgment on the matter in question." *Auer*, 519 U.S. at 462. In addition, unlike the situation in *Auer*, the agency here can claim no relevant expertise, as compared to the courts, as to limitations periods. *See Gonzales v. Oregon*, 546 U.S. 243, 256-57 (2006). Finally, deferring to an agency in these circumstances would raise serious separation-of-powers concerns by "permit[ting] the person who promulgates a law to interpret it as well." *Talk Am., Inc. v. Michigan Bell Tel. Co.*, 131 S. Ct. 2254, 2266 (2011) (Scalia, J., concurring); *see also* John F. Manning, *Constitutional Structure and Judicial Deference to Agency Interpretations of Agency Rules*, 96 Colum. L. Rev. 612 (1996).

C. In Any Event, The Regulation Is Invalid

Assuming that the regulation must be interpreted on its own terms to apply retroactively to the circumstances here, it is invalid.

1. If The Regulation Must Be Given Retroactive Effect, It Is *Ultra Vires*

An agency may not engage in retroactive lawmaking *at all* unless Congress has unmistakably authorized it to do so. *Bowen*, 488 U.S. at 208. Before 1996, Congress authorized the Commissioner "to correct any ruling, regulation, or Treasury decision retroactively, but empowered him, in his discretion, to *limit* retroactive application to the extent necessary to

avoid inequitable results." *Automobile Club of Michigan v. Comm'r*, 353 U.S. 180, 184 (1957) (emphasis added); *id.* (construing § 3791(b) of 1939 Code, now codified as relevant in 26 U.S.C. § 7805(b)(5)). That authority was generally designed to allow Treasury to *ameliorate* the otherwise retroactive effect of changes in its *own* internal rules. It does not authorize Treasury retroactively "to correct" a decision of *this* Court and then apply the new rule in a way that would create "inequitable results."

In 1996, Congress changed the law in a way that favors taxpayers and *restricts* the Commissioner's authority to promulgate retroactive rules. That year, Congress—while leaving § 7805(b)(5) in place—added a new provision (§ 7805(b)(1)) that generally prohibits retroactive regulations related to the tax laws with limited exceptions not relevant here. That prohibition reflects Congress's view that "it is generally inappropriate for Treasury to issue retroactive regulations." H.R. Rep. No. 104-506, at 44 (1996); *see* Benjamin J. Cohen & Catherine A. Harrington, *Is the Internal Revenue Service Bound by Its Own Regulations and Rulings?*, 51 Tax Law. 675, 698-99 (1998) (discussing legislative efforts to prohibit retroactive rulemaking by Treasury).

The 1996 amendments to § 7805 state that the new provisions "shall apply with respect to regulations which relate to statutory provisions enacted on or after the date of the enactment." Pub. L. No. 104-168, § 1101(b), 110 Stat. 1452, 1469 (1996); 26 U.S.C. § 7805 (note). The government argues that the old version of § 7805(b) applies to *all* post-1996 regulations, unless the underlying Code section was enacted after July 30, 1996. U.S. Br. 42-43. That reading would reduce to a

whimper Congress's stated intent generally to *prohibit* retroactive Treasury regulations affecting taxpayers.

The more natural reading—and the only reading that is consistent with Congress's stated intent and the distinction it drew between substantive tax regulations and those relating to internal agency matters—is that the phrase "enacted on or after" modifies "*regulations* related to statutory provisions"—not just "statutory provisions." *See Black's Law Dictionary* 1280 (9th ed. 2009) ("positive law" includes "enacted law—the codes statutes, and regulations"); *Burks v. United States*, 633 F.3d 347, 350 (5th Cir. 2011) ("recently enacted Treasury Regulations"); *Transpac Drilling Venture 1982-12 v. Comm'r*, 147 F.3d 221, 228 (2d Cir. 1998) ("other regulations enacted"); Internal Revenue Manual § 1.15.2.4 (Mar. 12, 2010), *available at* http://www.irs.gov/irm/part1/irm_01-015-002.html ("[s]pecific laws and regulations were enacted"). Thus, § 7805(b)(1) prohibits retroactivity as to all regulations enacted after July 30, 1996 if they relate to "statutory provisions"—as opposed to *internal* Treasury matters, where retroactivity is permitted.[18]

At a minimum, even if the Commissioner otherwise has statutory authority retroactively to enact the kind of regulation at issue, the Commissioner's attempt retroactively to change the law in the extraordinary circumstances here is an abuse of discretion—and thus *ultra vires*, *see Automobile Club of Michigan*, 353 U.S.

---

[18] Congress *has* authorized the IRS to "provide that any regulation may take effect or apply retroactively to prevent abuse." 26 U.S.C. § 7805(b)(3). But the agency did not attempt to invoke that authority in issuing the regulation here, and thus may not defend the regulation on that ground in this Court. *See SEC v. Chenery Corp.*, 318 U.S. 80, 95 (1943).

at 184-85—for the same basic reasons that the agency is not entitled to any deference in this case.

2. The Regulation Is Not Entitled To *Chevron* Deference

In any event, the regulation is not entitled to deference under *Chevron* and *Mayo Foundation for Medical Education & Research v. United States*, 131 S. Ct. 704, 711 (2011), for at least two reasons.

First, the regulation impermissibly attempts to dictate the outcome of pending litigation in which the agency is a party. This Court has long recognized that "[d]eference to what appears to be nothing more than an agency's convenient litigating position" is "entirely inappropriate." *Bowen*, 488 U.S. at 213; *see also Chock Full O'Nuts Corp. v. United States*, 453 F.2d 300, 303 (2d Cir. 1971). The history of the regulation at issue here makes clear that it was issued to advance the agency's litigating position in cases in which the agency was a party—and, indeed, was a transparent attempt to reverse the tide of one loss after another on its implausible reading of the statute in the face of this Court's construction of the same language in *Colony*.[19]

---

[19] This is not the first time that the Treasury has tried to utilize retroactive regulations to decide pending litigation in which it was a party. The Treasury issued Regulation § 1.752-6 in similar circumstances, in an attempt to expand the meaning of the term "liability" for purposes of § 752. Like the regulations at issue here, Regulation § 1.752-6 was almost uniformly rejected by the courts that considered it. *See, e.g., Murfam Farms, LLC v. United States*, 88 Fed. Cl. 516, 526 (2009); *Stobie Creek Invs., LLC v. United States*, 82 Fed. Cl. 636, 671 (2008), *aff'd*, 608 F.3d 1366 (Fed. Cir. 2010); *Sala v. United States*, 552 F. Supp. 2d 1167, 1197 (D. Colo. 2008); *Klamath Strategic Inv. Fund, LLC v. United States*, 440 F. Supp. 2d 608, 625 (E.D. Tex. 2006).

The government's reliance (at 39-40) on *Mayo*, *Smiley*, and *United States v. Morton*, 467 U.S. 822 (1984), is misplaced. None of those decisions involved a regulation that purported to change *well settled law* in the midst of litigation in which the agency was a party. *See Smiley*, 517 U.S. at 744 n.3 ("There might be substance to this point if the regulation replaced a prior agency interpretation—which, as we have discussed, it did not."); *see also Burks*, 633 F.3d at 360 n.9 (explaining that *Mayo* did not involve a situation where, "during the pendency of the suit, the treasury promulgated determinative, retroactive regulations following prior adverse judicial decisions on the identical legal issue."). Whatever leeway an agency has to issue regulations in the midst of pending litigation, the extraordinary agency conduct at issue here passes the breaking point.

Second, the agency's interpretation cannot be sustained under *Chevron* step two because the agency's stated rationale for its choice of "reasonable" interpretations is based on a mistaken premise. As explained above, this Court conclusively interpreted the key statutory language at issue here in *Colony*, rejecting the same arguments advanced by the agency in support of its regulations. Moreover, Congress, by its actions in the decades since *Colony*, has ratified this Court's statutory holding. Even assuming that the statute was susceptible to more than one reasonable interpretation at the time of *Colony*, it is not susceptible to the Commissioner's interpretation today—and therefore fails *Chevron*'s second step. If that step is to have any vitality, it should apply in this case to prevent the IRS's unreasonable action here.

3. The Regulation Is Procedurally Defective

The temporary regulation was issued without the requisite notice and comment—a practice Treasury apparently employs with some frequency. *See* Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack Of) Compliance With Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727, 1730 (2007). The regulation thus flouts the requirements of the Administrative Procedures Act (APA), 5 U.S.C. § 553.

The APA's notice-and-comment requirement is grounded on the commonsense notion that an agency should provide notice and obtain comments *before* deciding what rule is appropriate, and not to issue the rules first, only to go through the motions of notice and comment after the agency has made up its mind. Anyone familiar with the inertias of the administrative state knows that notice and comment is a virtually meaningless charade if carried out in such fashion. *Cf. Ramaprakash v. FAA*, 346 F.3d 1121, 1122 (D.C. Cir. 2003) ("Learned Hand once remarked that agencies tend to 'fall into grooves, and when they get into grooves, then God save you to get them out.") (Roberts, J.) (alteration and citation omitted). The fact that Congress authorized agencies to bypass the notice-and-comment requirement where immediate guidance is necessary underscores that Congress did not intend to authorize agencies to dispense with that requirement as they see fit in *non*-emergency circumstances like those the IRS faced in 2009. *See* 5 U.S.C. § 553(b)(B); *see generally* Br. of Prof. Hickman as *Amicus Curiae* in Support of Respondents.

III. THE COMMISSIONER HAS AMPLE TOOLS AT HIS DISPOSAL TO IDENTIFY AND TIMELY ADDRESS PERCEIVED TAX SHELTER TRANSACTIONS

The government's policy arguments for why it needed a six-year period here are better directed to Congress than this Court. They are also unpersuasive. As discussed, the extended six-year limitations period is designed to provide the IRS with additional time only where it "is at a special disadvantage in detecting errors" because "the return on its face provides no clue to the existence of the omitted item." *Colony*, 357 U.S. at 36. Here, the returns on their face disclosed all the facts necessary for the IRS to determine whether a closer look was warranted. *See supra* at 26-28. The problem was not the IRS's *inability* to detect clues from the returns; it was that the Commissioner's agents waited nearly six years before they even *examined* the returns. Add. 19a. In any event, Congress has provided the IRS with ample tools to address perceived tax-shelter transactions generally, and alleged Son-of-BOSS transactions, specifically.

The IRS has broad authority under the Code to prescribe the type and form of information that taxpayers must provide for virtually any transaction. *E.g.*, 26 U.S.C. § 6011(a) (requiring "a return or statement according to the forms and regulations prescribed by the [IRS]" that "shall include therein the information required by such forms or regulation"). The agency also has broad examination authority to obtain documents and sworn testimony from taxpayers and third parties. *E.g.*, 26 U.S.C. § 7602(a).

Moreover, Congress has enacted several provisions requiring taxpayers and their advisors to disclose

participation in listed transactions. *E.g.*, 26 U.S.C. §§ 6011, 6111, 6112, 6707, 6707A, 6708. Failure to comply with these reporting obligations extends the limitations period for assessment. For example, § 6501(c)(10) requires a taxpayer to self-report its participation in a listed transaction. The failure to self-report tolls the statute of limitations until such information is furnished to the IRS. Similarly, § 6501(c)(8) provides that in the case of information required to be reported with respect to certain foreign transactions, the statute of limitations for assessment of tax shall extend until three years "after the date on which the Secretary is furnished the information" required to be reported under such section." Section 7609(e) suspends the limitations period indefinitely if a taxpayer fails to respond to a summons issued in connection with a listed transaction.

More specifically, in the wake of "Son-of-BOSS," the IRS immediately took several steps to identify and address perceived tax-shelter transactions. For example, the IRS: (1) issued regulations modifying reporting obligations for listed transactions (Temp. Treas. Reg. § 1.6011-4T, *reprinted in* 67 Fed. Reg. 64,799, 64,802-05 (Oct. 22, 2002)); (2) issued letters to several parties that it believed had promoted Son-of-BOSS transactions (2001 TNT 250-1 (Dec. 28, 2001)); (3) issued a report to Treasury on listed transactions and Notice 2000-44 (2001 TNT 250-11 (Dec. 28, 2001)); (4) issued a Partnership Audit Technique Guide addressing tax shelters and Notice 2000-44 (2003 TNT 241-26 (Dec. 16, 2003)); and (5) issued a "Son-of-BOSS Toolkit" to its agents detailing how to identify the transactions on a tax return. The IRS took each of

these steps before April 2003, when the limitations period for the returns at issue here expired.

* * * * *

What the Commissioner has attempted to do here is truly remarkable: retroactively overrule a decision of this Court conclusively resolving the meaning of a statutory provision in order to enlarge a limitations period for the purpose of altering the course of ongoing litigation in which the agency is a party. As Judge Wilkinson aptly observed below, the government's position calls for "something of an inversion of the universe and to pass the point where the beneficial application of agency expertise gives way to a lack of accountability and risk of arbitrariness." Pet. App. 20a (concurring). Neither *Chevron* nor any other principle of agency deference provides any reason for this Court to countenance such an unsettling agency action.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be affirmed.

Respectfully submitted,

RICHARD T. RICE
Counsel of Record
C. MARK WILEY
MICHAEL R. CASHIN
ROBERT T. NUMBERS II
WOMBLE CARLYLE
SANDRIDGE & RICE LLP
One West Fourth Street
Winston-Salem, NC 27101
(336) 721-3600
rrice@wcsr.com

GREGORY G. GARRE
J. SCOTT BALLENGER
LORI ALVINO MCGILL
LATHAM & WATKINS LLP
555 11th Street, NW
Suite 1000
Washington, DC 20004
(202) 637-2207
gregory.garre@lw.com

ROGER J. JONES
ANDREW R. ROBERSON
LATHAM & WATKINS LLP
233 South Wacker Drive
Suite 5800
Chicago, IL 60606
roger.jones@lw.com

ADDENDUM

TABLE OF CONTENTS

Page

Statutory Provisions:

26 U.S.C. § 6501(e)(1)(A), (e)(2) (2000) 1a

26 U.S.C. § 6501(e)(1)(A), (e)(2) (1958) 3a

26 U.S.C. § 275(a), (c) (1940) 5a

26 U.S.C. § 61 (2006) 6a

26 U.S.C. § 22(a) (1940) 8a

26 U.S.C. § 7805(b)(1), (5), note (2006) 9a

26 U.S.C. § 6229((a), (c)(2) (1982) 11a

Pub. L. No. 99-514 § 2, 100 Stat. 2085, 2095 (1986) 12a

Regulatory Provisions:

Treas. Reg. § 301.6501(e)-1(a)(1), (e) (2010) 13a

Temp. Treas. Reg. § 301.6501(e)-1T (Sept. 2009) 15a

26 C.F.R. § 301.6501(e)-1(a) ((in effect from 1956 to Sept. 2009)) 17a

26 C.F.R. § 29.22(a)-5 (1949) 18a

Other:

IRS Examination Letter (Feb. 23, 2006) 19a

26 U.S.C. § 6501 (e)(1)(A), (e)(2) (2000)

§ 6501. Limitations on assessment and collection

* * *

(e) Substantial omission of items

Except as otherwise provided in subsection (c)—

(1) Income taxes

In the case of any tax imposed by subtitle A—

(A) General rule

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item.

* * *

(2) Estate and gift taxes

In the case of a return of estate tax under chapter 11 or a return of gift tax under chapter 12, if the taxpayer omits from the gross estate or from the total amount of the gifts made during the period for which the return was filed items includible in such gross estate or such total gifts, as the case may be, as exceed in amount 25 percent of the gross estate stated in the return or the total amount of gifts stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. In determining the items omitted from the gross estate or the total gifts, there shall not be taken into account any item which is omitted from the gross estate or from the total gifts stated in the return if such item is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item.

* * *

26 U.S.C. § 6501(e)(1)(A), (e)(2) (1958)

§ 6501. Limitations on assessment and collection.

* * *

(e) Omission From Gross Income.

Except as otherwise provided in subsection (c)—

(1) Income taxes.

In the case of any tax imposed by subtitle A—

(A) General rule.

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement

attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item.

* * *

(2) Estate and gift taxes.

In the case of a return of estate tax under chapter 11 or a return of gift tax under chapter 12, if the taxpayer omits from the gross estate or from the total amount of the gifts made during the year items includible in such gross estate or such total gifts, as the case may be, as exceed in amount 25 percent of the gross estate stated in the return or the total amount of gifts stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. In determining the items omitted from the gross estate or the total gifts, there shall not be taken into account any item which is omitted from the gross estate or from the total gifts stated in the return if such item is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item.

* * *

26 U.S.C. § 275(a), (c) (1940)

§ 275. Period of limitation upon assessment and collection.

Except as provided in section 276—

(a) General rule.

The amount of income taxes imposed by this chapter shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

* * *

(c) Omission from gross income.

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

* * *

26 U.S.C. § 61 (2006)

§ 61. Gross income defined

(a) General definition

Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, fringe benefits, and similar items;

(2) Gross income derived from business;

(3) Gains derived from dealings in property;

(4) Interest;

(5) Rents;

(6) Royalties;

(7) Dividends;

(8) Alimony and separate maintenance payments;

(9) Annuities;

(10) Income from life insurance and endowment contracts;

(11) Pensions;

(12) Income from discharge of indebtedness;

(13) Distributive share of partnership gross income;

(14) Income in respect of a decedent; and

(15) Income from an interest in an estate or trust.

(b) Cross references

For items specifically included in gross income, see part II (sec. 71 and following). For items specifically excluded from gross income, see part III (sec. 101 and following).

26 U.S.C. § 22(a) (1940)

§ 22. Gross income—(a) General definition.

"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and Judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such Presidents and judges are hereby amended accordingly. In the case of judges of courts of the United States who took office on or before June 6, 1932, the compensation received as such shall be included in gross income.

26 U.S.C. § 7805(b)(1), (b)(5), note (2006)

§ 7805. Rules and regulations

* * *

(b) Retroactivity of regulations

(1) In general

Except as otherwise provided in this subsection, no temporary, proposed, or final regulation relating to the internal revenue laws shall apply to any taxable period ending before the earliest of the following dates:

(A) The date on which such regulation is filed with the Federal Register.

(B) In the case of any final regulation, the date on which any proposed or temporary regulation to which such final regulation relates was filed with the Federal Register.

(C) The date on which any notice substantially describing the expected contents of any temporary, proposed, or final regulation is issued to the public.

* * *

(5) Internal regulations

The limitation of paragraph (1) shall not apply to any regulation relating to internal Treasury Department policies, practices, or procedures.

* * *

EFFECTIVE DATE OF 1996 AMENDMENT

Section 1101(b) of Pub. L. 104-168 provided that:

"The amendment made by subsection (a) [amending this section] shall apply with respect to regulations which relate to statutory provisions enacted on or after the date of the enactment of this Act [July 30, 1996]."

* * *

26 U.S.C. § 6229 (1982)

* * *

§ 6229. Period of limitations for making assessments

(a) General rule

Except as otherwise provided in this section, the period for assessing any tax imposed by subtitle A with respect to any person which is attributable to any partnership item (or affected item) for a partnership taxable year shall not expire before the date which is 3 years after the later of —

(1) the date on which the partnership return for such taxable year was filed, or

(2) the last day for filing such return for such year (determined without regard to extensions).

* * *

(c) Special rule in case of fraud, etc.

* * *

(2) Substantial omission of income.

If any partnership omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in its return, subsection (a) shall be applied by substituting "6 years" for "3 years".

* * *

Pub. L. No. 99-514, 100 Stat. 2085 (1986)

SEC. 2. INTERNAL REVENUE CODE OF 1986.

(a) REDESIGNATION OF 1954 CODE.—The Internal Revenue Title enacted August 16, 1954, as heretofore, hereby, or hereafter amended, may be cited as the "Internal Revenue Code of 1986".

(b) REFERENCES IN LAWS, ETC.—Except when inappropriate, any reference in any law, Executive order, or other document—

(1) to the Internal Revenue Code of 1954 shall include a reference to the Internal Revenue Code of 1986, and

(2) to the Internal Revenue Code of 1986 shall include a reference to the provisions of law formerly known as the Internal Revenue Code of 1954.

* * *

TREASURY REGULATION § 301.6501(e)-1 (2010)

§ 301.6501(e)-1 Omission from return.

(a) *Income taxes—(1) General rule.* (i) If a taxpayer omits from the *gross* income stated in the return of a tax imposed by subtitle A of the Internal Revenue Code an amount properly includible therein that is in excess of 25 percent of the gross income so stated, the tax may be assessed, or a proceeding in court for the collection of that tax may be begun without assessment, at any time within 6 years after the return was filed.

(ii) For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to a trade or business, means the total of the amounts received or accrued from the sale of goods or services, to the extent required to be shown on the return, without reduction for the cost of those goods or services.

(iii) For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to any income other than from the sale of goods or services in a trade or business, has the same meaning as provided under section 61(a), and includes the total of the amounts received or accrued, to the extent required to be shown on the return. In the case of amounts received or accrued that relate to the disposition of property, and except as provided in paragraph (a)(1)(ii) of this section, *gross income* means the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property. Consequently, except as provided in paragraph (a)(1)(ii) of this section, an understated amount of gross income resulting from an

overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A)(i).

* * *

(e) *Effective/applicability date*—(1) *Income taxes.* Paragraph (a) of this section applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009.

* * *

TEMPORARY TREASURY REGULATION § 301.6501(e)-1T (Sept. 2009)

§ 301.6501(e)-1T Omission from return (temporary).

(a) *Income taxes*—(1) *General rule.* (i) If the taxpayer omits from the gross income stated in the return of a tax imposed by subtitle A of the Internal Revenue Code an amount properly includible therein that is in excess of 25 percent of the gross income so stated, the tax may be assessed, or a proceeding in court for the collection of that tax may be begun without assessment, at any time within 6 years after the return was filed.

(ii) For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to a trade or business, means the total of the amounts received or accrued from the sale of goods or services, to the extent required to be shown on the return, without reduction for the cost of those goods or services.

(iii)For purposes of paragraph (a)(1)(i) of this section, the term *gross income*, as it relates to any income other than from the sale of goods or services in a trade or business, has the same meaning as provided under section 61(a), and includes the total of the amounts received or accrued, to the extent required to be shown on the return. In the case of amounts received or accrued that relate to the disposition of property, and except as provided in paragraph (a)(1)(ii) of this section, *gross income* means the excess of the amount realized from the disposition of the property over the unrecovered cost or other basis of the property. Consequently, except as provided in paragraph (a)(1)(ii) of this section, an understated amount of gross income resulting from an

overstatement of unrecovered cost or other basis constitutes an omission from gross income for purposes of section 6501(e)(1)(A).

(iv) An amount shall not be considered as omitted from gross income if information sufficient to apprise the Commissioner of the nature and amount of the item is disclosed in the return, including any schedule or statement attached to the return.

(2) [Reserved]

(b) *Effective/applicability date.* The rules of this section apply to taxable years with respect to which the applicable period for assessing tax did not expire before September 24, 2009.

(c) *Expiration date.* The applicability of this section expires on or before September 24, 2012.

26 C.F.R. § 301.6501(e)-1(a)
(in effect from 1956 to Sept. 2009)

§ 301.6501(e)–1 Omission from return.

(a) *Income taxes*—(1) *General rule.* (i) If the taxpayer omits from the gross income stated in the return of a tax imposed by subtitle A of the Code an amount properly includible therein which is in excess of 25 percent of the gross income so stated, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed.

(ii) For purposes of this subparagraph, the term "gross income", as it relates to a trade or business, means the total of the amounts received or accrued from the sale of goods or services, to the extent required to be shown on the return, without reduction for the cost of such sales or services. An item shall not be considered as omitted from gross income if information, sufficient to apprise the district director of the nature and amount of such item, is disclosed in the return or in any schedule or statement attached to the return.

* * *

26 C.F.R. § 29.22(a)-5 (1949)

§ 29.22(a)-5 *Gross income from business.* In the case of a manufacturing, merchandising, or mining business, "gross income" means the total sales, less the cost of goods sold, plus any income from investments and from incidental or outside operations or sources. In determining the gross income subtractions should not be made for depreciation, depletion, selling expenses, or losses, or for items not ordinarily used in computing the cost of goods sold. But see § 29.23 (m)-1(f).

* * *

Internal Revenue Service
Department of the Treasury

Date: February 23, 2006

Home Concrete & Supply, LLC
Robert L. Pierce TMP
2812 Shady Ave.
Wilmington, NC 28409

Taxpayer Identification Number:
56-2136387
Form:
1065
Tax Period(s):
1999
Person to Contact:
William C. Maier Jr.
Contact Telephone Number:
408.817.6307
Contact Fax Number:
408.817.6795
Employee Identification Number:
77-02014

Dear Mr. Pierce,

Your federal return for the period(s) shown above has been selected for examination.

What You Need To Do

Please call me on or before March 9, 2006. I can be contacted from 8am PST to 5pm PST at the contact telephone number provided above.

Letter 2205-A (Rev. 10-2005)
Catalog Number 37456E

What We Will Discuss

During our telephone conversation, we will discuss:

- Items on your return that I will be examining.
- Types of documentation I will ask you to provide.
- The examination process.
- Any concerns or questions you may have.
- The date, time and agenda for our first meeting.

The issues listed below are the preliminary items identified for examination. During the course of the examination, it may be necessary to expand or contract the list of items. If this should occur, I will advise you of the change.

- Notice 2000-44 Transaction • •
- • •

Someone May Represent You

You may have someone represent you during any part of this examination. If you want someone to represent you, please provide me with a completed Form 2848, *Power of Attorney and Declaration of Representative*, at our first appointment.

If you prefer, you may mail or fax the form to me prior to our first appointment. You can get this form from our office, or from our web site at www.irs.gov, or by calling 1-800-829-3676. If you decide that you wish to get representation after the examination has started, we will delay further examination activity until you can secure representation.

Letter 2205-A (Rev. 10-2005)
Catalog Number 37456E

Your Rights As A Taxpayer

We have enclosed Publication 1, *Your Rights as a Taxpayer*, and Notice 609, *Privacy Act Notice*. We encourage you to read the Declaration of Taxpayer Rights found in Publication 1. This publication discusses general rules and procedures we follow in examinations. It explains what happens before, during, and after an examination, and provides additional sources of information.

Thank you for your cooperation, and I look forward to hearing from you by March 9, 2006,

Sincerely,

s/ William C. Maier Jr.

William C. Maier Jr.
Internal Revenue Agent

Enclosures:
Publication 1
Notice 609
Form 4564 Information Document Request one

REPLY BRIEF

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

DONALD B. VERRILLI, JR.
Solicitor General
Counsel of Record
Department of Justice
Washington, D.C. 20530-0001
SupremeCtBriefs@usdoj.gov
(202) 514-2217

TABLE OF CONTENTS

Page

A. An overstatement of basis can trigger Section 6501(e)(1)(A)'s six-year assessment period 2
   1. The statutory text is naturally construed to encompass an understatement of gross income attributable to an overstatement of basis 2
   2. Statutory amendments enacted in 1954 reinforce the conclusion that an overstated basis can trigger the six-year period 3
   3. Congress has not acted since the 1954 amendments to change the general rule that an overstated basis can trigger the six-year period ... 7
   4. The statutory purpose strongly supports extending the period for discovery of a basis overstatement 11
B. The recent Treasury regulation resolves any statutory ambiguity by specifying that an overstatement of basis triggers the six-year assessment period 13
   1. *Colony* does not control the interpretation of current Section 6501(e)(1)(A) 13
   2. The final regulation was validly promulgated, applies to this case, and is entitled to deference .. 17
   3. The final regulation is not impermissibly retroactive 19

TABLE OF AUTHORITIES

Cases:

Automobile Club v. *Commissioner*, 353 U.S. 180 (1957) 20

Babbitt v. *Sweet Home Chapter of Cmtys. for a Great Or.*, 515 U.S. 687 (1995) 6

Cases—Continued: Page

Bakersfield Energy Partners, LP v. *Commissioner*:
128 T.C. 207 (2007), aff'd, 568 F.3d 767 (9th Cir. 2009) 15
568 F.3d 767 (9th Cir. 2009) 16
Benderoff v. *United States*, 398 F.2d 132 (8th Cir. 1968) 10
Bishop v. *United States*, 338 F. Supp. 1336 (N.D. Miss. 1970) 10
Brandon Ridge Partners v. *United States*, No. 8:06-1340, 2007 WL 2209129 (M.D. Fla. July 30, 2007) 15
Burks v. *United States*, 633 F.3d 347 (5th Cir. 2011), petition for cert. pending, No. 11-178 (filed Aug. 11, 2011) 15
CC & F W. Operations Ltd. P'ship v. *Commissioner*, 273 F.3d 402 (1st Cir. 2001) 17
Colony, Inc. v. *Commissioner*, 357 U.S. 28 (1958) ..... *passim*
Dixon v. *United States*, 381 U.S. 68 (1965) 20
Florida Dep't of Revenue v. *Piccadilly Cafeterias, Inc.*, 554 U.S. 33 (2008) 5
Grapevine Imports, Ltd. v. *United States*, 636 F.3d 1368 (Fed. Cir. 2011), petition for cert. pending, No. 11-163 (filed Aug. 5, 2011) 14, 20
Howard E. Clendenen, Inc. v. *Commissioner*, 207 F.3d 1071 (8th Cir. 2000) 21
Intermountain Ins. Serv. of Vail, LLC v. *Commissioner*, 650 F.3d 691 (D.C. Cir. 2011), petition for cert. pending, No. 11-663 (filed Nov. 16, 2011) ..... *passim*

Cases—Continued: Page

Mayo Found. for Med. Educ. & Research v. *United States*, 131 S. Ct. 704 (2011) 19
Myers v. *United States*, No. 71-126, 1972 WL 3167 (S.D. Cal. July 20, 1972) 10
National Cable & Telecomms. Ass'n v. *Brand X Internet Servs.*, 545 U.S. 967 (2005) 14
Phinney v. *Chambers*, 392 F.2d 680 (5th Cir.), cert. denied, 391 U.S. 935 (1968) 14, 15, 17
Quick's Trust v. *Commissioner*, 54 T.C. 1336 (1970) 10
Rhone-Poulenc Surfactants & Specialties, L.P. v. *Commissioner*, 114 T.C. 533 (2000), appeal dismissed, 249 F.3d 175 (3d Cir. 2001) 16
Russell F. Davis, Inc. v. *United States*, 170 F. Supp. 185 (N.D. Ind. 1959) 10
Salman Ranch, Ltd. v. *Commissioner*, 647 F.3d 929 (10th Cir. 2011), petition for cert. pending, No. 11-582 (filed Nov. 7, 2011) 14, 20
Smiley v. *Citibank (S.D.), N.A.*, 517 U.S. 735 (1996) 19
Talk Am., Inc. v. *Michigan Bell Tel. Co.*, 131 S. Ct. 2254 (2011) 18
United States v. *Morton*, 467 U.S. 822 (1984) 19
University Country Club, Inc. v. *Commissioner*, 64 T.C. 460 (1975) 10
William Thomas, 42 T.C.M. (P-H) ¶ 73,261 (1973) 16

Statutes and regulations:

Administrative Procedure Act, 5 U.S.C. 553 17
Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, Tit. VIII, § 810(b)(2), 79 Stat. 169 5

Statutes and regulations—Continued: Page

Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1101(b), 110 Stat. 1469 20
26 U.S.C. 63(a) 11
26 U.S.C. 117(1)(A) (1952) 8
26 U.S.C. 275(c) (1940) ..... *passim*
26 U.S.C. 743(b)(1) 12
26 U.S.C. 754 12
26 U.S.C. 1221(a)(1) 8
26 U.S.C. 6110(k)(3) 16
26 U.S.C. 6229(c)(2) 10
26 U.S.C. 6501(c)(10) 12
26 U.S.C. 6501(e) 5
26 U.S.C. 6501(e)(1) 5
26 U.S.C. 6501(e)(1)(A) ..... *passim*
26 U.S.C. 6501(e)(1)(A)(i) 5, 8, 10, 13
26 U.S.C. 6501(e)(1)(A)(ii) 10, 11, 12, 16
26 U.S.C. 6501(e)(1)(B) 4
26 U.S.C. 6501(e)(2) 4, 5, 8, 13
26 U.S.C. 6501(e)(3) 4, 5
26 U.S.C. 7805(b) (Supp. III 1956) 20
26 U.S.C. 7805(b)(8) (1996) 20
26 U.S.C. 7806(b) 5
74 Fed. Reg. 49,321 (Sept. 28, 2009) 10
Treas. Reg.:
§ 1.1221-1(b) 8
§ 301.6501(e)-1 13
§ 301.6501(e)-1(e) 17

Miscellaneous: Page

IRS GCM 36856, 1976 WL 39111 (1976) 16

John F. Manning, *Constitutional Structure and Judicial Deference to Agency Interpretations of Agency Rules*, 96 Colum. L. Rev. 612 (1996) 18

In the Supreme Court of the United States

No. 11-139

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

Respondents make little effort to tie their interpretation of 26 U.S.C. 6501(e)(1)(A) to the text of that provision. Rather, they rely on *Colony, Inc.* v. *Commissioner*, 357 U.S. 28 (1958) (*Colony*), which involved a predecessor statute rather than Section 6501(e)(1)(A) in its present form. Contrary to respondents' contentions, however, the statutory language has changed in important respects that the *Colony* Court had no occasion to consider, and the Court recognized in any event that the earlier version of the statute was ambiguous. Accordingly, neither text nor precedent foreclosed the Treasury Department from adopting, through notice-and-comment rulemaking, its current reasonable interpretation of the disputed statutory language.

A. An Overstatement Of Basis Can Trigger Section 6501(e)(1)(A)'s Six-Year Assessment Period

1. The statutory text is naturally construed to encompass an understatement of gross income attributable to an overstatement of basis

Under Section 6501(e)(1)(A), the Internal Revenue Service (IRS) has six years from the filing of a return to assess additional taxes "[i]f the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return." The amount of unreported income at issue here—approximately $6 million—is "in excess of 25 percent of the amount of gross income stated in the return." Thus, the only question is whether respondents "omit[ted]" that "amount" from their "gross income" when they (i) overstated their bases in Home Concrete, (ii) subtracted those inflated amounts from their shares of the sale proceeds, and (iii) thereby reported gains from the sale of Home Concrete that were a tiny fraction of their actual gains. If the statutory terms are given their ordinary meaning, the $6 million difference between respondents' actual capital gains and their reported gains is naturally treated as "an amount" that was "properly includible" (*i.e.*, that ought to have been included) in respondents' "gross income," but that respondents instead "omit[ted]."

Respondents omitted that amount from their gross income by overstating their bases in Home Concrete, no less than if they had understated the partnership's sales price. When a taxpayer reports the capital gains from a property sale on Schedule D of his tax return, he does so by listing the property, its "[c]ost or other basis," and its "[s]ales price." See, *e.g.*, J.A. 128. The taxpayer's capital gain is then calculated by subtracting the basis from the sales

price. *Ibid.* It therefore does not matter which variable—sales price or basis—a taxpayer misrepresents on his return: a misstatement in either column results in an omission of an amount of the taxpayer's gross income. See Gov't Br. 15-16, 19-20.

Respondents do not contend that Section 6501(e)(1)(A) distinguishes between overstatements of basis and understatements of sales price. Respondents argue instead that Section 6501(e)(1)(A) is inapplicable so long as a taxpayer reports the fact of a property sale and acknowledges that he received *some* gross income from it. In respondents' view, a taxpayer "omits from gross income an amount properly includible therein" only when "an *item* of gross income" is "left out entirely" from the return. Br. 37 (emphasis added). The ordinary meaning of the statute's terms does not support, much less compel, that limitation. See Gov't Br. 18-19. If a taxpayer sells property for $10 million but misrepresents the sales price to be $1 million, he is naturally described as "omit[ting] from gross income an amount [*i.e.*, $9 million] properly includible therein," just as if he had failed entirely to report a $9 million sale.

2. ***Statutory amendments enacted in 1954 reinforce the conclusion that an overstated basis can trigger the six-year period***

As respondents observe (Br. 23-25), the dispute between the parties in this case parallels to a significant degree the dispute concerning Section 6501(e)(1)(A)'s predecessor statute (26 U.S.C. 275(c) (1940)) that the Court resolved in *Colony*. The government argued in *Colony* that Congress's "use of the word 'amount' (instead of, for example, 'item') suggests a concentration on the quantitative aspect of the error—that is, whether or not gross income was understated by as much as 25%." 357 U.S. at 32. The taxpayer

countered that Congress's use of "the word 'omits,' * * * when it could have chosen another verb such as 'reduces' or 'understates,'" limited the statute "to situations in which specific receipts or accruals of income items are *left out* of the computation of gross income." *Id.* at 32-33.

The *Colony* Court stated that, although it was "inclined to think that the statute on its face lends itself more plausibly to the taxpayer's interpretation, it cannot be said that the language is unambiguous." 357 U.S. at 33. The Court therefore "turn[ed] to the legislative history of [Section] 275(c)," *ibid.*, and held that former Section 275(c) encompassed only "a taxpayer's omission to report some taxable item," *id.* at 36. In reaching that conclusion, however, the Court had no occasion to consider two changes that Congress had made to the statute in 1954. Those changes did not apply to the tax years at issue in *Colony*, but they provide strong contextual support for the government's reading of current Section 6501(e)(1)(A).

a. *First*, Congress added Section 6501(e)(2), which applies to estate and gift taxes and allows the IRS six years from the filing of a return to assess additional tax "if the taxpayer omits * * * *items* includible" in the gross estate. 26 U.S.C. 6501(e)(2) (emphasis added). Congress used the term "items" to indicate that, in the estate- and gift-tax contexts, the six-year period is not triggered by an alleged undervaluation of property. See Gov't Br. 23. By contrast, Sections 6501(e)(1)(A) and (B), which define the assessment period for income taxes, and Section 6501(e)(3), which defines the assessment period for excise taxes, all refer to the omission of "an amount" from gross income.

Respondents make no meaningful effort to explain why Congress would use the term "item" in some provisions and "amount" in others if it had intended for both terms to be given the same meaning. Instead, they argue (Br. 35 &

n.14) that in 1965, when Congress changed the heading of Section 6501(e) from "Omission from gross income" to "Substantial omission of items," it eliminated any distinction between omission of "amount[s]" and omission of "items." Excise Tax Reduction Act of 1965, Pub. L. No. 89-44, Tit. VIII, § 810(b)(2), 79 Stat. 169. Congress gave no reason for that "[c]lerical amendment" (*ibid.*) to the heading, however, and the general focus of the 1965 amendments was on the excise-tax provision in Subsection (e)(3) rather than the income-tax provision in Subsection (e)(1). In any event, "a sub[section] heading cannot substitute for the operative text of the statute." *Florida Dep't of Revenue* v. *Piccadilly Cafeterias, Inc.*, 554 U.S. 33, 47 (2008). Indeed, the Internal Revenue Code provides that "descriptive matter" relating to the Code's contents shall not be given "any legal effect." 26 U.S.C. 7806(b). The shorthand terminology used in Section 6501(e)'s heading therefore does not negate the inference that would otherwise naturally be drawn from Congress's use of different terms in Sections 6501(e)(1)(A) and 6501(e)(2).

b. *Second*, the 1954 amendments added subparagraph (i) of Section 6501(e)(1)(A), which provides that "[i]n the case of a trade or business, the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services * * * prior to diminution by the cost of such sales or services." 26 U.S.C. 6501(e)(1)(A)(i). At that time, the circuits were divided on whether a basis overstatement can give rise to an omission from gross income. See *Intermountain Ins. Serv. of Vail, LLC* v. *Commissioner*, 650 F.3d 691, 704-705 (D.C. Cir. 2011) (*Intermountain*), petition for cert. pending, No. 11-663 (filed Nov. 16, 2011); see also Gov't Br. 45-46. Virtually all of those lower-court cases involved trades or businesses that had overstated their cost of goods sold. See *id.* at 53 n.8. Congress

amended the statute to make clear that, for trade-or-business taxpayers, an overstatement of basis or cost of goods sold cannot trigger the six-year assessment period. The amendment would have been unnecessary if, as respondents contend, a basis overstatement cannot trigger the six-year period for *any* taxpayer.

Respondents argue that "[i]t is not unusual for Congress to spell out the application of a general rule to a specific fact pattern, even if there would be a belt[]-and-suspenders component to its action." Br. 31. In interpreting statutes, however, this Court typically presumes that Congress amends its handiwork for a real and substantial reason. See *Babbitt* v. *Sweet Home Chapter of Cmtys. for a Great Or.*, 515 U.S. 687, 701 (1995). The historical backdrop against which the 1954 Congress acted reinforces that normal inference. Although the pre-1954 cases involving basis overstatements typically involved trade-or-business taxpayers, former Section 275(c) did not distinguish between those taxpayers and others. By establishing a special rule for trade-or-business taxpayers, subparagraph (i) reflected a departure from Congress's prior approach to the definition of appropriate assessment periods. That special rule makes sense, because unlike the one-time transaction at issue here, trades and businesses engage in repeated and routine sales where the bases or costs of goods sold are often easier for the government to gauge and businesses' miscalculations could frequently give rise to the extended assessment period.

Respondents further argue that Congress could not have intended "to change the 'General rule' in former [Section] 275(c) that it left untouched by adding a subparagraph addressing only a particular situation." Br. 32. The government's position in this case, however, does not depend on the premise that the 1954 Congress *intentionally* changed

the law with respect to non-trade-or-business taxpayers. Congress enacted the 1954 amendments four years before this Court's decision in *Colony*. As explained above, those amendments contained provisions that would be anomalous if the omission of an *item* of gross income were necessary to trigger Section 6501(e)(1)(A)'s six-year assessment period. The most natural inference is that Congress believed in 1954 that non-trade-or-business taxpayers were *already* subject to the extended assessment period if they substantially understated their gross income, including by overstating their bases in sold property. To be sure, the Court in *Colony* subsequently determined that this reading of former Section 275(c) was incorrect. But the 1954 Congress's apparent misunderstanding of pre-1954 law provides no legitimate ground for refusing to consider the full statutory context in construing current Section 6501(e)(1)(A).

3. Congress has not acted since the 1954 amendments to change the general rule that an overstated basis can trigger the six-year period

This Court in *Colony* observed, with respect to the phrase "omits from gross income an amount properly includible therein" in former Section 275(c), that "it cannot be said that the language is unambiguous." 357 U.S. at 33. After resolving that ambiguity in the taxpayer's favor, the Court noted at the end of its opinion that its conclusion was "in harmony with the unambiguous language of [Section] 6501(e)(1)(A) of the Internal Revenue Code of 1954." *Id.* at 37. In an accompanying footnote, the Court reproduced the text of the amended provision, including subparagraph (i). *Id.* at 37 n.3.

In characterizing new Section 6501(e)(1)(A) as "unambiguous," the *Colony* Court could not have been referring to the portion of the text that was common to both the 1939

and 1954 Codes. That reading would mean that "within the span of just four pages of the U.S. Reports," the Court described the same language "as both ambiguous and unambiguous." *Intermountain*, 650 F.3d at 703. Rather, it makes far more sense to read the concluding reference to "the unambiguous language of [Section] 6501(e)(1)(A)" as an allusion to new subparagraph (i). Subparagraph (i) prevents an overstatement of the cost of goods or services sold by a trade or business like Colony from triggering the six-year period, because such an overstatement does not affect the calculation of the trade-or-business taxpayer's gross income. The Court's disposition of *Colony* therefore was "in harmony with" the outcome that Section 6501(e)(1)(A)(i) would have mandated. 357 U.S. at 37.[1]

For that reason, respondents are wrong in suggesting (Br. 33) that Congress's failure to amend Section 6501(e)(1)(A) in the years since *Colony* supports their position. By enacting new subparagraph (i) four years before the *Colony* decision, Congress had already made clear that post-1954 trade-or-business taxpayers should for these purposes be treated differently from other post-1954 taxpay-

---

[1] The taxpayer at issue in *Colony* was a real estate developer that was subdividing farm land into residential lots and selling those lots to individual buyers. Respondents' contention (Br. 32 & n.7) that *Colony* did not involve the sale of goods by a trade or business is therefore misplaced. Although land is not normally considered a good, when property is held by a taxpayer primarily for sale to customers in the ordinary course of the taxpayer's trade or business, those transactions are treated for tax purposes as sales of goods rather than as sales of capital assets. See 26 U.S.C. 1221(a)(1); Treas. Reg. 1.1221-1(b); 26 U.S.C. 117(1)(A) (1952). Consistent with that principle, the taxpayer in *Colony*, both on its tax returns and during the litigation before the Tax Court, "described itself as a taxpayer in a trade or business with income from the sale of goods or services." *Intermountain*, 650 F.3d at 703; see Gov't Br. 52-53.

ers. *Colony* itself involved a business entity, and the Court's observation about the manner in which the case would have been decided under the 1954 amendments is best understood as reflecting awareness of that specific provision. And while subparagraph (i) makes clear that an overstatement of basis cannot trigger the six-year assessment period in the trade-or-business context, both subparagraph (i) and Section 6501(e)(2) indicate that a different rule applies to non-trade-or-business taxpayers. See pp. 4-7, *supra*. Because the Court in *Colony* had no occasion to consider the application of then-new Section 6501(e)(1)(A) to taxpayers other than trades or businesses, Congress's failure to amend the provision in subsequent years does not support respondents' position. See *Intermountain*, 650 F.3d at 705.[2]

Respondents assert that "[w]hen Congress reenacted [Section] 6501 as part of the 1986 Code, it did so against the backdrop" of "cases applying *Colony*'s holding" to Section 6501(e)(1)(A). Br. 33. But none of the cases that respondents cite (see *id.* at 33 n.13) addressed the question whether an overstatement of basis triggers the extended six-year assessment period in Section 6501(e)(1)(A). They all addressed the distinct question whether a taxpayer that had omitted a substantial amount of gross income from his return could nevertheless invoke the statutory safe harbor for disclosure because his return was "adequate to apprise the

---

[2] As in *Colony*, resolution of the question presented here would be easier if Section 6501(e)(1)(A) either required the omission of an "item" of gross income or applied by its terms to "understatements" of gross income. See 357 U.S. at 32-33; pp. 3-4, *supra*. But the recognition that Congress could have spoken more clearly is the beginning rather than the end of the interpretive inquiry.

Secretary of the nature and amount of [the omitted] item," 26 U.S.C. 6501(e)(1)(A)(ii).[3]

In 1982, Congress enacted a parallel provision for partnership returns, 26 U.S.C. 6229(c)(2), which applies when "any partnership omits from gross income an amount properly includible therein." That provision is not at issue here because this case involves only omissions from individual partners' returns (subject to Section 6501(e)(1)(A)) and not omissions from Home Concrete's partnership return (subject to Section 6229(c)(2)). Respondents suggest (Br. 34-35), however, that because Section 6229(c)(2) lacks any analogue to subparagraph (i) of Section 6501(e)(1)(A), subparagraph (i) must not be germane to Section 6501(e)(1)(A)'s proper construction. That argument lacks merit.

When Congress enacted Section 6229(c)(2), it adopted the same general rule as in Section 6501(e)(1)(A) and reasonably presumed that the two provisions would be interpreted *in pari materia*. See *Intermountain*, 650 F.3d at 705. The Treasury Department has adopted that approach, see Pet. App. 51a-52a, to ensure that partners are not "treated differently based on the happenstance of whether the transaction is reported on a partnership return rather than on a partner's return." 74 Fed. Reg. 49,321 (Sept. 28, 2009). No canon of statutory construction required the Department either to give different meanings to Sections 6229(c)(2) and Section 6501(e)(1)(A) or to ignore probative

---

[3] See *Benderoff* v. *United States*, 398 F.2d 132, 135 (8th Cir. 1968); *Myers* v. *United States*, No. 71-126, 1972 WL 3167, at *10 (S.D. Cal. July 20, 1972); *Bishop* v. *United States*, 338 F. Supp. 1336, 1349 (N.D. Miss. 1970); *University Country Club, Inc.* v. *Commissioner*, 64 T.C. 460, 469 (1975); *Quick's Trust* v. *Commissioner*, 54 T.C. 1336, 1346 (1970); cf. *Russell F. Davis, Inc.* v. *United States*, 170 F. Supp. 185, 186 (N.D. Ind. 1959) (addressing a basis misstatement under former Section 275(c)).

contextual evidence bearing on the proper construction of Section 6501(e)(1)(A).

4. The statutory purpose strongly supports extending the period for discovery of a basis overstatement

a. Relying on *Colony*, respondents argue (Br. 24-25) that there is no reason to treat an overstated basis differently from an overstated deduction, which can also be difficult to detect. Contrary to respondents' suggestion (*ibid.*), however, the difference in treatment does not create any "patent incongruity" in the tax laws. *Colony*, 357 U.S. at 36. Although overstatements of basis and overstatements of deductions may both result in understatement of *taxable* income, only the former can affect the taxpayer's calculation of *gross* income. And the distinction between the two concepts is deeply ingrained in the Internal Revenue Code. See, *e.g.*, 26 U.S.C. 63(a). In limiting Section 6501(e)(1)(A)'s six-year assessment period to cases involving substantial omissions from "gross income," Congress chose to encompass only a subset of all cases in which a taxpayer substantially understates his taxable income. But since overstatements of basis *do* result in omissions from gross income, Congress's decision not to sweep more broadly provides no justification for declining to give the statutory text its natural meaning.

b. Respondents contend (Br. 26-29) that their own returns demonstrate the absence of any need for an extended assessment period because those returns gave the IRS all the information it needed to evaluate respondents' gross-income calculations. Even where Section 6501(e)(1)(A)'s general rule applies, however, subparagraph (ii) renders the six-year period inapplicable if the omitted amount was adequately disclosed on the return or on an attached statement. See Gov't Br. 24-25. The district court found that

respondents could not take advantage of that safe harbor because their returns did not adequately disclose the substance of their transactions. See J.A. 98-112. The court of appeals did not overturn that conclusion, and respondents have not urged the Court to affirm the judgment below on the alternate ground that subparagraph (ii) was satisfied.[4] As the case comes to this Court, it must therefore be assumed that respondents did *not* sufficiently apprise the IRS of the omitted $6 million in capital gains.

Respondents also assert that the IRS "waited nearly six years" before examining their returns. Br. 51. The extended assessment period, however, is not limited to cases in which the IRS requires additional time to discover a taxpayer's misstatements *once the IRS has focused upon the taxpayer's return.* In this case, as in many Son-of-BOSS and other tax-shelter cases, the IRS focused on particular taxpayers only after (and because) the tax-shelter promoter identified those taxpayers as shelter participants. In such circumstances, Section 6501(e)(1)(A) increases the likelihood that the period for assessing additional tax will remain open when the IRS receives information that causes it to investigate a return that, on its face, gave the agency no reason to believe that substantial amounts of gross income had been omitted.[5]

---

[4] Although the individual partners' returns disclosed "a short sale not closed by the taxpayer," Resp. Br. 28 (quoting J.A. 204, 258; emphasis omitted), the returns did not alert the IRS that the partners had transferred to the Home Concrete partnership the obligation to close the short sale. And nothing on Home Concrete's return indicated that its "step up" in its basis—which is permissible in many circumstances, see 26 U.S.C. 743(b)(1), 754—was tied to the partners' asymmetric treatment of the short sale transactions.

[5] In 2004, Congress amended the statute to address transactions that the IRS has identified as tax-avoidance transactions, see 26 U.S.C.

B. The Recent Treasury Regulation Resolves Any Statutory Ambiguity By Specifying That An Overstatement Of Basis Triggers The Six-Year Assessment Period

Respondents make little effort to show that the recent Treasury regulation, Treas. Reg. 301.6501(e)-1, reflects an unreasonable interpretation of the statutory text. Rather, respondents and their amici argue that *Colony* left no statutory ambiguity for the government to resolve; that until recently the government had treated *Colony* as dispositive of the question presented here; and that in any event the regulation was invalidly promulgated, does not apply to this case, and is impermissibly retroactive. Those arguments lack merit.

1. Colony does not control the interpretation of current Section 6501(e)(1)(A)

a. The Court in *Colony* did not decide the meaning of Section 6501(e)(1)(A), which did not apply to the tax years at issue in that case. See 357 U.S. at 32, 37. Because the Court construed the statute as it existed before the 1954 amendments, it did not consider the implications of current Sections 6501(e)(1)(A)(i) and 6501(e)(2) for the interpretation of the extended-assessment-period provision. The statutory context has changed since *Colony*, and those changes bear on the proper interpretation of current Section 6501(e)(1)(A). See *Intermountain*, 650 F.3d at 703. By contrast, in adopting the recent regulation, the Treasury Department could consider the implications of adjacent statutory provisions that the *Colony* Court had no occasion to address.

6501(c)(10), but that amendment does not apply to this case (or any other pending Son-of-BOSS case, as far as the government is aware). See Gov't Pet. Reply Br. 4-5.

In any event, only a judicial decision "hold[ing] that its construction follows from the unambiguous terms of the statute" "displaces a conflicting agency construction." *National Cable & Telecomms. Ass'n* v. *Brand X Internet Servs.*, 545 U.S. 967, 982-983 (2005). The Court in *Colony* found the text of former Section 275(c) to be ambiguous. And "[a]lthough the Court found 'persuasive' evidence in the legislative reports * * *, it did not hold there was no other reasonable interpretation of the history." *Salman Ranch, Ltd.* v. *Commissioner*, 647 F.3d 929, 938 (10th Cir. 2011) (*Salman Ranch II*) (quoting *Colony*, 357 U.S. at 33), petition for cert. pending, No. 11-582 (filed Nov. 7, 2011); see *Intermountain*, 650 F.3d at 702; *Grapevine Imports, Ltd.* v. *United States*, 636 F.3d 1368, 1379 (Fed. Cir. 2011) (*Grapevine*) (same), petition for cert. pending, No. 11-163 (filed Aug. 5, 2011). *Colony* is thus precisely the sort of judicial construction of an ambiguous statute that does *not* foreclose a different agency interpretation.

b. Respondents contend (Br. 42) that for a half-century after *Colony*, until the extensive litigation over Son-of-BOSS shelters, it was well settled that a basis overstatement could not trigger the extended six-year assessment period. None of the pre-2009 decisions that respondents cite for that proposition (Br. 42 n.16), however, held that a basis overstatement could not trigger the six-year period. Rather, so far as the government is aware, *Phinney* v. *Chambers*, 392 F.2d 680 (5th Cir.), cert. denied, 391 U.S. 935 (1968), was the only pre-2009 court of appeals decision that addressed the application of Section 6501(e)(1)(A) to an understatement of gross income that resulted from an overstatement of basis. In *Phinney*, a return filed on behalf of the taxpayer accurately reported the amount of a particular gross receipt, but misrepresented that amount to be the proceeds of a sale of stock rather than (as was actually the

case) a receipt from the collection of a note evidencing an installment sale. See *id.* at 682. The return also reported a stepped-up basis equal to the purported stock-sale price (approximately $375,000) and therefore reported no taxable gain on that amount. *Id.* at 682, 685.

Relying on *Colony*, the taxpayer contended that the six-year assessment period was inapplicable because, "so long as the gross amount reported was not in error, there was no omission of 'an amount' from the return at all." *Phinney*, 392 F.2d at 685. In rejecting that interpretation of Section 6501(e)(1)(A), the court of appeals explained that, due to the return's mischaracterization of the nature of the income item (*i.e.*, as a receipt from a stock sale rather than from an installment note), the government had been denied an adequate opportunity to contest the taxpayer's claim to a stepped-up basis. See *id.* at 684-685. The court in *Phinney* did not announce a categorical rule that an "omi[ssion] from gross income" occurs whenever an overstatement of basis results in an understatement of gross income. Cf. *Burks* v. *United States*, 633 F.3d 347, 355 (5th Cir. 2011), petition for cert. pending, No. 11-178 (filed Aug. 11, 2011). But the court clearly viewed Section 6501(e)(1)(A) as applicable to at least some overstatement-of-basis cases, and it rejected the taxpayer's contention that accurate reporting of an amount of gross receipts forecloses application of the six-year assessment period.

It was then nearly 40 years before any court held that an overstated basis cannot trigger the six-year period. See *Bakersfield Energy Partners, LP* v. *Commissioner*, 128 T.C. 207 (2007), aff'd, 568 F.3d 767 (9th Cir. 2009); but see *Brandon Ridge Partners* v. *United States*, No. 8:06-1340, 2007 WL 2209129, at *8 (M.D. Fla. July 30, 2007) (holding that an overstated basis can trigger the six-year period). And while the Ninth Circuit in *Bakersfield* con-

cluded that *Colony*'s holding applies to the current Section 6501(e)(1)(A), the court suggested that, because the Court in *Colony* had found the language of former Section 275(c) to be ambiguous, "[t]he IRS may have the authority to promulgate a reasonable reinterpretation of an ambiguous provision of the tax code." 568 F.3d at 778. The IRS therefore moved to promulgate such regulations, first in temporary and then in final form, while the lower courts continued to reach differing conclusions over whether a basis overstatement can give rise to an omission from gross income.[6]

---

[6] Respondents cite (Br. 9, 42) two internal IRS documents—a 1976 General Counsel memorandum and a 2000 memorandum from district counsel in Philadelphia—in which the IRS purportedly took a different view of Section 6501(e)(1)(A). By statute, and as the concluding sentences of the documents themselves recite, those memoranda "may not be used or cited as precedent." 26 U.S.C. 6110(k)(3); see *Rhone-Poulenc Surfactants & Specialties, L.P.* v. *Commissioner*, 114 T.C. 533, 543 (2000), appeal dismissed, 249 F.3d 175 (3d Cir. 2001). In any event, neither document addressed the question whether a basis overstatement can give rise to an omission from gross income. And the 1976 General Counsel memorandum quoted with apparent approval a Tax Court decision specifically rejecting the proposition that "if a *type* of income is revealed in a tax return, there is sufficient disclosure, even though the amount is understated." IRS GCM 36856, 1976 WL 39111, at 11 (quoting *William Thomas*, 42 T.C.M. (P-H) ¶ 73,261, at 1190 (1973)). Although the documents cited *Colony* as relevant to the interpretation of Section 6501(e)(1)(A), that provision includes subparagraph (ii), the safe harbor for disclosure. Because *Colony* addressed the adequacy of disclosure under former Section 275(c), the decision has been cited extensively in litigation involving current Section 6501(e)(1)(A)(ii). See pp. 9-10 & n.3, *supra*.

2. The final regulation was validly promulgated, applies to this case, and is entitled to deference

a. Respondents argue (Br. 50) that the Treasury Department's temporary regulation was procedurally invalid under the Administrative Procedure Act, 5 U.S.C. 553, because it was adopted without notice-and-comment procedures. But the temporary regulation is not at issue here. In December 2010, after notice-and-comment rulemaking, the Department withdrew the temporary regulation and replaced it with the current final rule. See *Intermountain*, 650 F.3d at 709. Even assuming that an earlier procedural violation could conceivably taint the final rule, but see *ibid.*, the Department's "searching consideration" of the single comment that it received during the comment period leaves "no doubt that [it] kept the requisite open mind." *Id.* at 709-710 (internal quotation marks and citation omitted).

b. This case is governed by the final regulation, which "applies to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009." Treas. Reg. 301.6501(e)-1(e). Respondents do not dispute that the determination whether the period was "open" depends on whether the IRS had three or six years to assess additional income taxes. Rather, respondents argue (Br. 39-40) that this Court must ignore the regulation's substantive provisions in construing the rule's applicability clause, because it was settled law at the time the regulation was adopted that *Colony* dictated a three-year period. That argument rests on a mistaken premise. "Because *Colony* never applied to [S]ection 6501(e)(1)(A) * * *, there was no *settled* law for the regulations to change." *Intermountain*, 650 F.3d at 709; see *CC & F W. Operations Ltd. P'ship* v. *Commissioner*, 273 F.3d 402, 406 n.2 (1st Cir. 2001) ("Whether *Colony*'s main holding carries over to [S]ection 6501(e)(1) is at least doubtful."); *Phinney*,

392 F.2d at 684-685. Indeed, an important purpose of the final rule was to clarify the proper resolution of several pending cases that had produced disagreement in the lower courts.

In arguing that the final rule does not apply to this case, respondents ignore not only the regulation's substantive provisions but also the Treasury Department's interpretation of the regulation's applicability clause. In the preamble to the final regulation, the Department explained that, in determining whether the "period for assessing tax * * * was open on or after September 24, 2009," the relevant "period for assessing tax" in cases involving basis overstatement is six rather than three years because "[t]he expiration of the three-year period does not 'close' a taxable year if a longer period applies." Pet. App. 63a; see *Intermountain*, 650 F.3d at 708. Respondents contend that "the agency here can claim no relevant expertise, as compared to the courts, as to limitations periods." Br. 45. But the Department has obvious expertise in clarifying the intended temporal coverage of its own regulation, and the subject matter of the rule (which defines the period within which the IRS may make an *administrative* assessment of additional tax, rather than the period within which suit may be filed in court) is likewise squarely within the agency's sphere of authority. Deference to the Department's interpretation of the applicability clause is particularly appropriate because the Department issued that explanation contemporaneously with the rule itself, in the *Federal Register* preamble. Deferring to such a contemporaneous agency clarification cannot "encourage[] the agency to enact vague rules which give it the power, in future adjudications, to do what it pleases." *Talk Am., Inc.* v. *Michigan Bell Tel. Co.*, 131 S. Ct. 2254, 2266 (2011) (Scalia, J., concurring); cf. John F. Manning, *Constitutional Structure and Judicial Defer-*

ence to Agency Interpretations of Agency Rules, 96 Colum. L. Rev. 612, 689-690 (1996).

c. Respondents argue that the final rule is not entitled to deference because it "impermissibly attempts to dictate the outcome of pending litigation in which the agency is a party." Br. 48. This Court has made clear, however, that *Chevron* deference is not rendered inappropriate simply because it was litigation, including litigation to which the agency was a party, that disclosed the need for a regulation. See *Mayo Found. for Med. Educ. & Research* v. *United States*, 131 S. Ct. 704, 712 (2011); *Smiley* v. *Citibank (S.D.), N.A.*, 517 U.S. 735, 741 (1996); *United States* v. *Morton*, 467 U.S. 822, 836 n.21 (1984). Respondents attempt to distinguish *Mayo*, *Smiley*, and *Morton* on the ground that those cases did not "involve[] a regulation that purported to change *well settled law*." Br. 49. But if (as the government contends) the Treasury Department's construction of Section 6501(e)(1)(A) is not foreclosed by *Colony*, neither precedent nor logic suggests that lower-court decisions adverse to the government can deprive a reasonable agency interpretation of the deference to which it would otherwise be entitled. In any event, Section 6501(e)(1)(A)'s application to cases involving basis overstatements was unsettled when the regulation was adopted, and the rule resolved that uncertainty by codifying the interpretation that the Treasury Department had consistently advanced in prior adjudicative proceedings.

3. The final regulation is not impermissibly retroactive

Respondents also argue (Br. 40-43) that the final regulation is impermissibly retroactive. In this and similar cases involving Son-of-BOSS shelters, however, the Treasury Department has consistently maintained that it has six years to assess additional taxes when a taxpayer omits a

substantial amount from his gross income by overstating his basis in property. The purpose of the regulation was not to change the law, but simply to codify the Department's pre-existing interpretation of Section 6501(e)(1)(A). Moreover, the regulation does not bear on the legality of respondents' primary conduct, but simply clarifies the procedural rules governing enforcement of respondents' pre-existing tax liabilities.

In any event, the Treasury Department is authorized to "prescribe the extent, if any, to which any ruling or regulation, relating to the internal revenue laws, shall be applied *without retroactive effect*." 26 U.S.C. 7805(b) (Supp. III 1956) (emphasis added).[7] Under Section 7805(b), a regulation applies retroactively unless the Department in its discretion decides otherwise. See *Dixon* v. *United States*, 381 U.S. 68, 79-80 (1965); *Automobile Club* v. *Commissioner*, 353 U.S. 180, 184 (1957). To the extent that the final regulation at issue here has any retroactive effect, it is a permissible exercise of the Department's authority to promulgate retroactive rules. See *Salman Ranch II*, 647 F.3d at 943; *Grapevine*, 636 F.3d at 1382.

In 1996, Congress amended Section 7805(b) to limit the Treasury Department's authority to adopt regulations with retroactive effect, but those amendments apply only "with respect to regulations which relate to statutory provisions enacted on or after the date of the enactment of this Act." Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1101(b), 110 Stat. 1469. That limitation is not relevant here because the regulation at issue relates to 26 U.S.C. 6501(e)(1)(A), which was enacted as part of the 1954 amendments to the Code. The 1996 legislation did not limit the Department's

---

[7] In its opening brief (at 42), the government mistakenly cited 26 U.S.C. 7805(b)(8) (1996), rather than 26 U.S.C. 7805(b) (Supp. III 1956), as the applicable statute in this case.

authority to promulgate retroactive rules relating to pre-existing statutes. See, *e.g.*, *Howard E. Clendenen, Inc.* v. *Commissioner*, 207 F.3d 1071, 1074 (8th Cir. 2000).

* * * * *

For the foregoing reasons and those stated in our opening brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

DONALD B. VERRILLI, JR.
Solicitor General

JANUARY 2012

AMICUS CURIAE BRIEF

No. 11-139

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,
RESPONDENTS

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF OF THE GOVERNMENT OF THE UNITED STATES VIRGIN ISLANDS AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

VINCENT F. FRAZER
Attorney General
CAROL THOMAS-JACOBS
TAMIKA M. ARCHER
Assistant Attorneys General
Virgin Islands Department of Justice
GERS Complex
34-38 Kronprindsens Gade
St. Thomas, U.S.V.I. 00802
(340) 774-5666

GENE C. SCHAERR
Counsel of Record
LINDA T. COBERLY
PETER N. HIEBERT
BARRY J. HART
ADÈLE A. KEIM
Winston & Strawn LLP
1700 K Street, N.W.
Washington, DC 20006
(202) 282-5000
gschaerr@winston.com

Counsel for Amicus Curiae

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

QUESTION PRESENTED

Whether the Internal Revenue Service has validly abrogated this Court's holding in *Colony, Inc.* v. *Commissioner*, 357 U.S. 28 (1958)—that an overstatement of the basis of sold property is not an "omission" from gross income—and retroactively reopened and extended the statute of limitations applicable to respondents' tax returns.

TABLE OF CONTENTS

QUESTION PRESENTED i

TABLE OF CONTENTS ii

TABLE OF AUTHORITIES iv

INTRODUCTION AND INTERESTS OF AMICUS CURIAE 1

STATEMENT OF THE CASE 2

SUMMARY OF THE ARGUMENT 4

ARGUMENT 6

I. A Deferential Approach To Interpreting The Statute of Limitations Will Likely Have Substantial Adverse Effects On Programs Authorized by Congress and Relied Upon By State and Territorial Governments. 6

A. The IRS's arbitrary and retroactive changes to the statute of limitations can significantly undermine tax policies adopted by Congress and relied upon by state or territorial governments. 6

B. The V.I. Government currently faces serious adverse consequences as a result of the IRS's protracted audits of U.S.V.I. taxpayers who participated in its Congressionally-authorized economic development program—audits that have been made possible only by the IRS's overreaching and retroactive view of the statute of limitations. 11

II. The Statute Of Limitations Provisions In Section 6501 Have Been Carefully Crafted By Congress To Balance The IRS's Need For Time To Enforce The Tax Laws And The Taxpayer's Need For Repose 15

A. This Court has long regarded the tax statute of limitations as a matter of fundamental fairness..... 15

B. Rather than giving the IRS the ability to retroactively change the statute of limitations applicable to whole classes of transactions, Congress has chosen to give the IRS unlimited time to assess taxes in cases where a taxpayer has failed to file a return or has filed a fraudulent return..... 17

III. Even If The IRS Had Authority To Adopt A Rule Applying The Six-Year Statute of Limitations In This Case, That Rule Could Not Be Applied Retroactively. 19

A. Because it implicates matters of fundamental fairness, the statute of limitations is not a mere procedural rule that can be changed without regard to its retroactive effect. 20

B. The IRS abused its discretion in applying the regulation in this case retroactively. 21

CONCLUSION 22

TABLE OF AUTHORITIES

Page(s)

CASES

Abramson Enterprises, Inc. v. *Government of the Virgin Islands*, 994 F.2d 140 (3d Cir. 1993) 11, 12

Anderson, Clayton & Co. v. *United States*, 562 F2d 972 (5th Cir. 1977) 21

Appleton v. *Commissioner*, No. 7717-10 (T.C.) 12, 13

Appleton v. Commissioner, 430 F. App'x 135 (3d Cir. 2011) 14

Automobile Club of Michigan v. *Commissioner*, 353 U.S. 180 (1957) 21

Bakersfield Energy Partners, LP v. *Commissioner*, 568 F.3d 767 (9th Cir. 2009) 3

Bizcap, Inc. v. *Olive*, 892 F.2d 1163 (3d Cir. 1989) 11

Central Ilinois Public Service Co. v. *United States*, 435 U.S. 21 (1978) 21, 22

Chenault v. *U.S. Postal Service*, 37 F.3d 535 (9th Cir. 1994) 19, 20

Coffey v. Commissioner, No. 11-1362, --- F.3d ---, 2011 WL 6004080 (8th Cir. Dec. 2, 2011) 14

Colony, Inc. v. *Commissioner*,
357 U.S. 28 (1958) ..... i, 3, 17, 22

CWT Farms, Inc. v. *Commissioner*,
755 F.2d 790 (11th Cir. 1985) 21

Frank Lyon Co. v. *United States*,
435 U.S. 561 (1978) 10

Fredericks v. Commissioner,
126 F.3d 433, (3d Cir. 1997) 16, 17

Gehl Co. v. *Commissioner*,
795 F.2d 1324 (7th Cir. 1986) 10, 21

Historic Boardwalk Hall, LLC v. *Commissioner*,
136 T.C. 1, 26 (2011) 9, 10

Home Concrete & Supply, LLC v. *United States*,
634 F.3d 249 (4th Cir. 2011) 3

Hughes Aircraft Co. v. *U.S. ex rel. Schumer*,
520 U.S. 939 (1997) 19, 20

Intermountain Insurance Service of Vail v.
Commissioner,
134 T.C. 211 (2010) 17

Intermountain Insurance Service of Vail v.
Commissioner,
650 F.3d 691 (D.C. Cir. 2011) 3, 14, 17

Khoury v. *Commissioner*,
No. 10291-09 (T.C.) 13, 14

Landgraf v. *USI Film Products*,
511 U.S. 244 (1994) 20

LeCroy Research System Corp. v. *Commissioner*,
751 F.2d 123 (2d Cir. 1984) 4, 10, 11, 21

Lindh v. *Murphy*,
521 U.S. 320 (1997) 20

Rothensies v. *Electric Storage Battery Co.*,
329 U.S. 296 (1946) 5, 15, 22

Sacks v. *Commissioner*,
69 F.3d 982 (9th Cir. 1995) 9

Snap-Drape Inc. v. *Commissioner*,
98 F.3d 194 (5th Cir. 1996) 21

South Carolina v. *Baker*,
485 U.S. 505 (1988) 7

South Carolina v. *Regan*,
465 U.S. 367 (1984) 7

STATUTES

26 U.S.C. § 934 13

26 U.S.C. § 6011 18

26 U.S.C. § 6501 ..... *passim*

26 U.S.C. § 6501a 1, 4

26 U.S.C. § 6501c 2, 18, 22

26 U.S.C. § 6501e 3, 6, 17, 19

26 U.S.C. § 7805 21

American Jobs Creation Act of 2004, Pub. L. No. 108–357, § 814(a), 118 Stat. 1418 18

Community Renewal Tax Relief Act of 2000, Pub. L. No. 106-554, 114 Stat. 2763 8

Revenue Act of 1918, Pub. L. No. 65-254, § 250(d), 40 Stat. 1057 16

Tax Relief and Health Care Act of 2006, Pub. L. No. 109-432, 120 Stat. 2922 8

Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1101(a), 110 Stat. 1452 (1996) 21

The Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users, Pub. L. No. 109-59, 119 Stat. 1144 (2005) 8

OTHER MATERIALS

Treasury Regulation § 1.932-1(c) 12, 14

Treasury Regulation § 1.6091-3(c) 14

Treasury Regulation § 301.6501(e)-1 ..... 3, 5, 19

Supreme Court Rule 37.6 1

IRS Notice 2000-44, 2000-2 C.B. 255 (published Sept. 5, 2000) 2

IRS Chief Counsel Advice 200624002 (published June 16, 2006) 12

IRS Form 1040 Instructions (2006) 12, 14

IRS Pub. 570, Tax Guide for Individuals With Income From United States Possessions (2006) 12

67 Congressional Record 2961 (Jan. 29, 1926) 16

67 Congressional Record 3852 (Feb. 12, 1926) 16

Joint Comm. on Taxation, 112th Cong., Background Information on Tax Expenditure Analysis and Historical Survey of Tax Expenditure Estimates (Feb. 28, 2011) ... 4, 6, 7, 8, 9

INTRODUCTION AND INTERESTS OF *AMICUS CURIAE*[1]

Amicus Government of the United States Virgin Islands ("V.I. Government") appears before the Court principally to address one narrow but important issue: the impact that the IRS's gamesmanship on the statute of limitations can have, not just on private taxpayers, but also on state, local and territorial governments.

In the case of the U.S. Virgin Islands ("U.S.V.I."), the IRS has relied on a retroactive and narrow *reinterpretation* of the three-year statute of limitations in Section 6501(a) of the Internal Revenue Code (26 U.S.C. §§ 1 *et seq.*, hereafter "Code") to seriously undermine a V.I. Government tax incentive program—a program authorized by Congress since 1960 to encourage economic development in the Islands. The IRS accomplished this by effectively suspending the Section 6501(a) statute of limitations for U.S.V.I. taxpayers who in certain tax years followed federal statutes and IRS guidance and filed their tax returns with the V.I. Government. As a result of the IRS's suspension of that statute of limitations, hundreds of these taxpayers have been caught up in IRS audits lasting six years or longer. As a result, many have ended their participation in the V.I. Government's tax incentive program—and many have left the U.S.V.I. with their businesses—thereby frustrating

---

[1] The parties have consented to the filing of this brief, and their letters of consent are on file with the Clerk. In accordance with Rule 37.6, the V.I. Government states that no counsel for any party has authored this brief in whole or in part, and no person or entity, other than the V.I. Government, has made a monetary contribution to the preparation or submission of this brief.

Congress' policy objectives and seriously harming the U.S.V.I. economy.

By unilaterally reinterpreting the statute of limitations applicable to entire categories of taxpayers in the U.S.V.I. and in this case, the IRS is acting outside its Congressionally-authorized authority. Congress, moreover, has already given the IRS the ability to assess taxes without limit where the taxpayer failed to file any return, or where the taxpayer has filed a false or fraudulent return. Section 6501(c)(1), (2), (3). And if the IRS needs more time to carry out an audit on a particular taxpayer, Congress has authorized it to extend the statute of limitations by agreement with the taxpayer. Section 6501(c)(4). But what Congress has *not* done is grant the IRS *carte blanche* to unilaterally change the statute of limitations applicable to certain types of transactions, and then apply its new rule retroactively.

The IRS's arbitrary behavior in this case and others like it undermines taxpayer confidence in the U.S. government and ultimately undercuts the effectiveness of tax policies adopted by Congress and local governments. The V.I. Government urges this Court to reject the IRS's arguments and affirm the decision below.

STATEMENT OF THE CASE

In the early 2000s, the IRS began to crack down on a sophisticated and abusive tax shelter known as "Son of BOSS," which relied on overstating the taxpayer's basis in certain property in order to understate his income. IRS Notice 2000-44, 2000-2 C.B. 255 (published Sept. 5, 2000). But the IRS ran out of time to carry out all the audits it wished to conduct, and it started issuing assessments under the six-year

statute of limitations in Section 6501(e)—which applies where there has been an "omission from gross income"—instead of the normal three-year statute of limitations in Section 6501(a). See, e.g., *Bakersfield Energy Partners, LP* v. *Comm'r*, 568 F.3d 767, 778 (9th Cir. 2009). Shortly thereafter, the IRS began applying the Section 6501(e) statute of limitations to other taxpayers who were *not* accused of participating in any kind of abusive tax shelter and who had fully reported their gross income, but who still (in the IRS's view) overstated their basis in sold property. See *Intermountain Ins. Serv. of Vail* v. *Comm'r*, 650 F.3d 691, 694 (D.C. Cir. 2011).

When taxpayers who received untimely IRS tax assessments began to challenge the IRS in court, the IRS defended its position that Section 6501(e) applied – notwithstanding the fact that this application of Section 6501(e) was squarely rejected by this Court in *Colony* v. *Commissioner*, which interpreted a prior version of the same statute. *Home Concrete & Supply, LLC* v. *United States*, 634 F.3d 249, 253-55 (4th Cir. 2011) (citing *Colony*, 357 U.S. 28 (1958)).

After the IRS lost in the Ninth Circuit, the IRS promulgated a regulation expressly adopting its rejected litigation position, and sought to apply its brand-new regulation to other cases pending in the federal courts. Treas. Reg. § 301.6501(e)-1; see *Home Concrete & Supply, LLC*, 634 F.3d at 255-56 (citing *Bakersfield Energy Partners*, 568 F.3d at 778). After the Fourth Circuit rejected the IRS's attempt to rely on the retroactive application of its new regulation in this case, the IRS sought and obtained a writ of certiorari from this Court. IRS Br. at 1-2.

SUMMARY OF THE ARGUMENT

When the IRS makes arbitrary and retroactive changes to the statute of limitations, it affects not just individual taxpayers, but also state, local, and territorial governments whose revenues are directly or indirectly affected by federal tax policy.

1. Congress has enacted dozens of tax incentive programs designed to benefit state, local and territorial communities by "encourage[ing] activities which * * * may have been underprovided by the market in the absence of a subsidy provided by the Federal Government." Joint Comm. on Taxation, 112th Cong., Background Information on Tax Expenditure Analysis and Historical Survey of Tax Expenditure Estimates at 13 (Feb. 28, 2011) (hereafter "Tax Expenditure Analysis"). The IRS's administrative treatment of those tax incentives – and its decision to change the rules regarding those tax incentives retroactively – can have an enormous impact on their effectiveness and viability, because "[a]n ongoing power to dishonor deliberately created expectations will deter private parties from seeking to take advantage of proffered tax benefits designed to encourage particular economic activity." *LeCroy Research Sys. Corp.* v. *Comm'r* 751 F.2d 123, 128 (2d Cir. 1984).

That is the case in the U.S.V.I., where the IRS's decision to disregard the Section 6501(a) statute of limitations for certain U.S.V.I. taxpayers has all but destroyed the V.I. Government's Congressionally-authorized, tax incentive-based economic development program. That is because the IRS's decision has enabled the IRS to carry out endless audits of participating taxpayers, which in turn has caused

many existing participants to leave and deterred new ones from joining the program.

2. This Court has long regarded the tax statute of limitations as a matter of fundamental fairness to taxpayers. *Rothensies* v. *Elec. Storage Battery Co.*, 329 U.S. 296, 301 (1946). But the IRS's position in this case is fundamentally at odds with the balance that Congress struck in Section 6501 between the taxpayer's need for repose and the IRS's need for adequate time to carry out its audits. Congress has given the IRS a set of powerful tools in Section 6501, including the ability to assess taxes without any time limit in cases where the taxpayer has filed a false or fraudulent return, and the power to extend the limitations period by agreement in cases where it simply needs more time. What Congress has *not* done is give the IRS *carte blanche* to change the limitations period applicable to entire categories of taxpayers, and then apply that change retroactively.

3. Because the Section 6501 statute of limitations implicates matters of fundamental fairness, it is not the kind of merely procedural rule that can be applied to pending cases without raising concerns about retroactivity. Indeed, even assuming the IRS is correct that it has the authority to apply its 2010 regulation retroactively, it was still an abuse of its discretion for it to do so here. The result of the IRS's position is that the taxpayers here, who have not been accused of failing to file or of filing a false or fraudulent return, are still litigating their 1999 tax liability in 2011. That is exactly the outcome Congress sought to prevent when it adopted the Section 6501 statute of limitations. This Court should rebuke the IRS and affirm the Fourth Circuit's ruling below.

ARGUMENT

I. A Deferential Approach To Interpreting The Statute of Limitations Will Likely Have Substantial Adverse Effects On Tax Incentive Programs Authorized by Congress and Relied Upon By State, Local and Territorial Governments.

The IRS's decision to unilaterally change its longstanding position on the statute of limitations in a case such as this one can have a significant impact on the other governments that must coordinate their own programs with the federal tax system. Taxpayers who know that the IRS may retroactively change fundamental rules like the statute of limitations are far less likely to alter their behavior in response to government tax incentives. Thus, when considering whether and to what extent to defer to the IRS's interpretation of Section 6501(e), this Court should bear in mind that the IRS has sought to reinterpret other parts of Section 6501 as well, and carefully consider the potential impact of its ruling in this case on other governmental bodies.

A. The IRS's arbitrary and retroactive changes to the statute of limitations can significantly undermine tax policies adopted by Congress and relied upon by state or territorial governments.

State and territorial tax systems and economies are highly dependent upon the federal income tax system. For example, the federal tax exclusion for interest on state and local government debt has appeared among the top ten corporate "tax expenditures" since 1975, and in 2010-14 it was projected to

top $45.3 billion.[2] Tax Expenditure Analysis at 17, 25, Tbl. 8. The federal tax deduction for nonbusiness state and local taxes is even larger, and in 2010-14 is projected to reach more than $237.3 billion. *Id.*

Because of the interdependent nature of local and federal taxes, federal tax law can, and at times does, "materially interfere with and infringe upon the authority" of state, local and territorial governments to raise revenue and develop local economies. *South Carolina* v. *Regan,* 465 U.S. 367, 382 (1984). Thus, federal laws regarding bond interest may force states to issue bonds in the IRS's preferred form or risk losing investors who are seeking to minimize their federal tax liability by taking advantage of the federal deduction for state and local bonds. See *id.*; see also *South Carolina* v. *Baker,* 485 U.S. 505, 527 (1988) (upholding bond interest laws against state constitutional challenge). In short, what the IRS does when enforcing federal tax law can have a direct and substantial impact on state and territorial revenues. However, as the *South Carolina* cases illustrate, it can be extremely difficult for local governments to challenge IRS regulations or policies which threaten those revenues. See *South Carolina,* 465 U.S. at 380-81 (concluding that the Anti-Injunction Act did not bar South Carolina's constitutional challenge to a tax statute that allegedly affected its ability to raise rev-

---

[2]As used in this brief, a "tax expenditure" or tax incentive includes "any reductions in income tax liabilities that result from special tax provisions or regulations that provide tax benefits to particular taxpayers." Joint Comm. on Taxation, Background Information on Tax Expenditure Analysis and Historical Survey of Tax Expenditure Estimates at 2 (Feb. 28, 2011).

enues because the state lacked alternative avenues for challenging the law).

1. Many federal tax incentives "were enacted specifically to encourage activities which * * * may have been underprovided by the market in the absence of a subsidy provided by the Federal Government." Tax Expenditure Analysis at 13. Providing these incentives through the tax system has disadvantages (for example, it tends to make the tax code more complex), but it also offers "speed and dependability" and "an administrative mechanism[that is] already in place, reaching a large majority of the American public." *Id.* at 15. As a result, Congress has often used tax incentives to carry out policies that directly benefit state, territorial, or local governments by, for example:

- Encouraging investment in impoverished communities through the new markets tax credit (Community Renewal Tax Relief Act of 2000, incorporated by reference in the Consolidated Appropriations Act-FY 2001, Pub. L. No. 106-554, 114 Stat. 2763);
- Encouraging investment state and local infrastructure by excluding interest on qualified bonds for highway projects (The Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users, Pub. L. No. 109-59, 119 Stat. 1144 (2005)); and
- Encouraging investment in U.S. possessions by, for example, creating tax credits for corporate income earned in American Samoa (Tax Relief and Health Care Act of 2006, Pub. L. No. 109-432, 120 Stat. 2922).

The Joint Committee on Taxation estimates that, as of 2007, Congress had enacted over 200 different tax incentives (Tax Expenditure Analysis at 16 fig. 1), and it shows no sign of abandoning these important policy tools. Moreover, more than 31 of the federal tax incentives enacted since 1986 alone have directly or indirectly impacted state, local, territorial, or tribal governments. Addendum Tbl. 1.

2. The IRS's *administrative* treatment of those tax incentives can have a large impact on their effectiveness and viability. This is no less true of federal tax incentives designed to further specific federal policies than it is of incentives aimed primarily at facilitating state and federal government's attempts to raise revenue.

Sometimes, unfortunately, the IRS acts as though it simply disagrees with the policy choice Congress has made. In some cases, for example, the IRS has flatly refused to recognize transactions involving federal tax credits designed to create incentives for businesses to invest in otherwise unprofitable endeavors such as historic preservation. Thus, in *Sacks* v. *Commissioner*, the IRS argued that it should be able to exclude Congressionally-authorized environmental tax credits if it concluded that the underlying transaction lacked "economic substance." 69 F.3d 982, 992 (9th Cir. 1995). The Ninth Circuit rejected the IRS's argument, pointing out that "[i]f the government treats tax-advantaged transactions as shams unless they make economic sense on a pre-tax basis, then it takes away with the executive hand what it gives with the legislative." *Id.* And in *Historic Boardwalk Hall, LLC* v. *Commissioner*, the Tax Court rejected the IRS's allegation that a particular transaction involving federal tax credits for the rehabilitation of

historic properties lacked economic substance, because creating incentives to engage in otherwise unprofitable historic renovations was exactly the reason that Congress created the tax credits in the first place. 136 T.C. 1, 26 (2011) ("Congress enacted the rehabilitation tax credit in order to spur private investment in unprofitable historic rehabilitations."). These decisions are consistent with this Court's recognition that, because "the tax laws affect the shape of nearly every business transaction," the mere "fact that favorable tax consequences were taken into account by [the taxpayer] on entering into [a] transaction is no reason for disallowing those consequences." *Frank Lyon Co.* v. *United States*, 435 U.S. 561, 580 (1978).

The IRS's opposition to federal tax incentives can also take *indirect* forms, as when it retroactively changes the rules applicable to certain kinds of transactions. Retroactive rule changes like the ones in this case are particularly devastating to tax incentives, because "[i]f a taxpayer knows that the Treasury's promise that a new Code provision designed to encourage certain behavior will not be adversely altered retroactively is an illusory promise," then "that taxpayer will surely be less likely to alter his behavior in the manner hoped for by Congress when it passed the particular provision," and "[f]uture attempts to reduce the cost of uncertainty for taxpayers will prove ineffective at best." *Gehl Co.* v. *Commissioner*, 795 F.2d 1324, 1334 (7th Cir. 1986). Indeed, "[a]n ongoing power to dishonor deliberately created expectations will deter private parties from seeking to take advantage of proffered tax benefits designed to encourage particular economic activity," and "[w]hatever revenue enhancement may occur by al-

lowing retroactive application of this regulation today would thus be at the cost of diminishing Congress's power to use the tax code to create quasi-regulatory incentives tomorrow." *LeCroy Research Sys.*, 751 F.2d at 128. Simply stated, if taxpayers believe that claiming benefits offered under a Congressionally authorized tax incentive program is likely to provoke a negative reaction from the IRS—direct or indirect—they are far less likely to participate.

Thus, the retroactive application of the statute of limitations in this case will likely have implications far beyond the listed transactions at issue here, and ultimately make it more difficult for Congress and lawmakers in state and territorial governments to raise revenue and achieve their policy goals through tax incentives.

B. The V.I. Government currently faces serious adverse consequences as a result of the IRS's protracted audits of U.S.V.I. taxpayers who participated in its Congressionally-authorized economic development program—audits that have been made possible only by the IRS's overreaching and retroactive view of the statute of limitations.

The V.I. Government's situation illustrates the devastating impact that the IRS's recent reinterpretation of the statute of limitations can have on other tax sovereigns. Since at least 1954, U.S.V.I. residents have generally satisfied their federal tax liability by filing with and paying their taxes to the V.I. Government's Bureau of Internal Revenue ("Bureau"). *Bizcap, Inc.* v. *Olive*, 892 F.2d 1163, 1165 (3d Cir. 1989); *Abramson Enters., Inc.* v. *Gov't of the V.I.*,

994 F.2d 140, 144 (3d Cir. 1993) (noting that the "Virgin Islands is not a state," and as a general matter, "its citizens do not pay taxes to the IRS"). What is more, U.S.V.I. residents use the same forms that U.S. citizens on the mainland use when filing their tax returns with the IRS. See, e.g., IRS Form 1040 Instructions (2006) (instructing U.S.V.I. residents to file their Form 1040 with the Bureau); IRS Pub. 570, Tax Guide for Individuals With Income From United States Possessions (2006) at 14-15 (same).

Starting in 2006, however, the IRS embarked on a remarkable set of administrative actions culminating in a final 2008 regulation that refused to recognize *any* pre-December 31, 2006 federal tax returns filed with the Bureau by U.S. citizens reporting $75,000 or more in gross income – even if the IRS received a copy of these tax returns from the Bureau as part of the routine exchange of information between the two taxing authorities. IRS Chief Counsel Advice 200624002 (published June 16, 2006); Treas. Reg. § 1.932-1(c)(2)(ii); see V.I. Gov't Am. Mot. for Sum. J. at 4-5, *Appleton* v. *Comm'r*, No. 7717-10 (T.C. Nov. 28, 2011) (noting that the Bureau forwarded a copy of the taxpayer's return to the IRS). The IRS takes the position that these taxpayers have simply "failed to file" a tax return, a position which has allowed the IRS to claim that it has an unlimited time to assess taxes under Section 6501(c)(3). See IRS Answer at 6-7, *Appleton* v. *Comm'r*, No. 7717-10 (T.C. May 25, 2010) (alleging failure to file a federal tax return; admitting that returns were filed with the Bureau). The IRS has used this administrative fiction to keep hundreds of current and former U.S.V.I. residents tied up in audits that have lasted in many cases for six or more years. V.I. Gov't Surreply in Support of Mot. to In-

tervene Ex. B at 2, *Appleton* v. *Comm'r*, No. 7717-10 (T.C. Oct. 19, 2010) (letter from the Department of the Treasury to Sen. Charles Grassley noting that 260 of the U.S.V.I. taxpayers under IRS audit in 2007 were affected by the IRS's position on the statute of limitations).

The IRS's gamesmanship has had a devastating impact on the U.S.V.I. economy, which is heavily dependent on a Congressionally-authorized tax incentive program authorized designed to attract business investment to the Islands. 26 U.S.C. § 934; see V.I. Gov't Reply in Support of Mot. to Intervene Ex. B at 1-2, *Appleton* v. *Comm'r*, No. 7717-10 (T.C. Aug. 20, 2010) (Aug. 19, 2010 Declaration of Percival Clouden). As a result of the IRS's actions, hundreds of businesses have left the U.S.V.I., and it has become extremely difficult to attract new ones. V.I. Gov't Reply in Support of Mot. to Intervene Ex. A at 1-2, *Khoury* v. *Comm'r*, No. 10291-09 (T.C. Dec. 16, 2011) (Dec. 15, 2011 Declaration of Percival Clouden).

But the IRS has steadfastly refused to recognize the damage that its actions have caused to the U.S.V.I.'s economic development programs. Indeed, it has consistently opposed the V.I. Government's efforts simply to intervene in U.S. Tax Court proceedings to support individual U.S.V.I. taxpayers whose cases raise legal issues of importance to the V.I. Government. See, e.g., IRS Mot. for Leave to File Obj. to Mot. to Intervene at 1-2, *Khoury* v. *Comm'r*, No. 10291-09 (T.C. Nov. 10, 2011) (noting cases in which the IRS has opposed the V.I. Government's motion to

intervene in Tax Court proceedings on the statute of limitations).[3]

As in this case, the IRS has applied its new interpretation of the statute of limitations across the board without regard to whether the taxpayers participated in the V.I. economic development programs that the IRS now regards as suspect. See Treas. Reg. § 1.932-1(c)(2)(ii); *cf. Intermountain Ins. Serv. of Vail*, 650 F.3d at 694. Unlike the taxpayers here, however, the overwhelming majority of U.S.V.I. taxpayers caught up in the IRS's statute of limitations time warp are *not* accused of participating in "listed" transactions that the IRS deems abusive. Their only "mistake" was to follow federal statutes and published IRS guidance instructing them to file their tax returns with the V.I. Government rather than the IRS. See, e.g., Treas. Reg. § 1.6091-3(c) (instructing "citizens of a possession of the United States" to file their federal tax returns at the place designated in the IRS tax return forms or instructions); IRS Form 1040 Instructions (2006) (instructing permanent residents of the Virgin Islands to file their federal returns by sending them to the "V.I. Bureau of Internal Revenue, 9601 Estate Thomas, Charlotte Amalie, St. Thomas, VI 00802").

Nevertheless, the IRS continues to insist that, for these taxpayers, it has unlimited time to assess taxes and, thus, to continue its audits. And the agency

---

[3] So far, both federal courts of appeals to address the IRS's objections to intervention have overruled them, and have ordered the Tax Court to allow intervention by the V.I. Government. See *Appleton v. Commissioner* (*Appleton II*), 430 F. App'x 135 (3d Cir. 2011); *Coffey v. Commissioner*, No. 11-1362, --- F.3d ---, 2011 WL 6004080 (8th Cir. Dec. 2, 2011).

does so in the face of the substantial economic damage its position has inflicted and continues to inflict on the U.S.V.I. economy, and on the very economic development program authorized by Congress to facilitate the Islands' self-sufficiency.

II. As Written, The Statute Of Limitations Provisions In Section 6501 Have Been Carefully Crafted By Congress To Balance The IRS's Need For Time To Enforce The Tax Laws And The Taxpayer's Need For Repose.

As with the IRS's position on the application of the statute of limitations to U.S.V.I. residents, the IRS's insistence on an extended statute of limitations in this case it is particularly puzzling in light of Congress' longstanding policy favoring clear rules of repose for taxpayers on the one hand, and the fact that Congress has *already* given the IRS ample authority to extend the statute of limitations in compelling situations.

A. This Court has long regarded the tax statute of limitations as a matter of fundamental fairness.

As this Court has long recognized, "a statute of limitation is an almost indispensable element of fairness as well as of practical administration of an income tax policy." *Rothensies*, 329 U.S. at 301. Indeed, "[i]t probably would be all but intolerable * * * to have an income tax system under which there never would come a day of final settlement," a system that "required both the taxpayer and the Government to stand ready forever and a day to produce vouchers, prove events, establish values and recall details of all that goes into an income tax contest." *Id.* Thus, for nearly a century, Congress has included statutes of

limitations in the federal income tax statutes. See, e.g., Revenue Act of 1918, Pub. L. No. 65-254, § 250(d), 40 Stat. 1057, 1083 (noting the five-year limitation included in the Revenue Act of 1918). And for nearly that long, Congress has responded sternly when the IRS has failed to complete its work in the time Congress has given it.

For example, in 1926 Congress was alarmed by the number of assessments — many going back as far as 1917 — that were outstanding under previous income tax laws and the emergency tax measures passed during World War I. 67 Cong. Rec. 2961 (Jan. 29, 1926). Senator Ashurst, during a 1926 debate on an amendment to reduce the statute of limitations, declared that "[i]t is a foul injustice to the citizens of the country to require them to pay their taxes and then for years thereafter require them to be uncertain as to whether they reached a finality with their Government." 67 Cong. Rec. 3852 (Feb. 12, 1926) (statement of Sen. Ashurst).

Given this strong Congressional policy, it is not surprising that lower courts have been quick to reject attempts by the IRS to unfairly evade the statute of limitations through administrative machinations. Thus, in *Fredericks* v. *Commissioner*, the Third Circuit held that the IRS was estopped from relying on a taxpayer's statute of limitations waiver form when the IRS lost the form and then failed to tell the taxpayer that it was found, preventing him from rescinding it. 126 F.3d 433, 451 (3d Cir. 1997). *Fredericks* emphasized that the IRS had no "ability to trump an act of Congress, to wit, the statute of limitations," and that the court's ruling was necessary to protect "citizens' interests in some minimum standard of decency, honor, and reliability in their relations with

their Government." *Id.* at 438 (internal quotations omitted).

Here, the IRS's argument amounts to a claim that it "lost" the correct interpretation of this Court's decision in *Colony* for over forty years, only to "recover" it (in a more expansive form) in the face of its own administrative need. But the IRS's assertion that the overstatement of basis like the one alleged in this case "can be extremely difficult to detect" (IRS Br. at 27) does not justify departing from the plain language of Section 6501(e)—which this Court in *Colony* concluded plainly focused on "omissions from gross income"—not on alleged miscalculations of net income. See Home Concrete Br. at 22-24.

B. Rather than giving the IRS the ability to retroactively change the statute of limitations applicable to whole classes of transactions, Congress has chosen to give the IRS unlimited time to assess taxes in cases where a taxpayer has failed to file a return or has filed a fraudulent return.

The IRS's position in this case is based largely on the "wishful notion" that its retroactive changes to the Section 6501(e) statute of limitations should apply because "[the taxpayer] was involved in what [the IRS] believes was an abusive transaction." *Intermountain Ins., Serv. Of Vail, LLC* v. *Comm'r*, 134 T.C. 211, 219 (2010) (*en banc*), *rev'd* 650 F.3d 691 (D.C. Cir. 2011). The V.I. Government agrees with the IRS that Son of BOSS transactions are abusive and impermissible. But the IRS's argument (at 25-27) that it needs to retroactively extend the Section 6501(e) statute of limitations to address these transactions is misguided.

First, Congress has already given the IRS ample latitude to combat intentional tax evasion. For example, the IRS may assess a deficiency at any time when it identifies:

- A "false or fraudulent return" that is filed "with the intent to evade tax;"
- A "willful attempt in any manner to defeat or evade" certain taxes; or
- A taxpayer who failed to file a return.

Sections 6501(c)(1), (2),(3). If the IRS believed any of these things was present here, it could seek to assess taxes without regard for when the taxpayer filed (or failed to file) a return. *Id.*

Second, in Section 6011, Congress gave the IRS the authority to require taxpayers to provide it with all the information it deems necessary to effectively detect and combat tax evasion. See Home Concrete Br. at 51-52.

Third, in case the IRS finds itself in need of additional time to audit a particular taxpayer, Congress has given the IRS the ability to *extend* the statute of limitations by agreement. Section 6501(c)(4).

Moreover, recent history demonstrates that, if the IRS feels that it needs additional time to evaluate particular kinds of transactions, Congress is more than willing to amend Section 6501 to accommodate it. In 2004, for example, Congress gave the IRS more time to assess taxes against taxpayers who fail to self-report their participation in certain transactions that the IRS listed as potentially abusive tax shelters. See American Jobs Creation Act of 2004 (JOBS Act), Pub. L. No. 108–357, § 814(a), 118 Stat. 1418, 1581.

Thus, not only is the IRS's Section 6501 toolbox already full of effective ways of extending or suspending the statute of limitations altogether, but the IRS may always return to Congress if it feels the need for a new tool. What the IRS may not do, however, is unilaterally reinterpret the laws that Congress has already passed, and retroactively apply them to a whole new class of taxpayers, as it did in this case—and as it has done in the U.S.V.I. taxpayer cases described above.

III. Even If The IRS Had Authority To Adopt A Rule Applying The Six-Year Statute of Limitations In This Case, That Rule Could Not Be Applied Retroactively.

Setting aside the unreasonableness of the IRS's Section 6501(e) reinterpretation, the IRS should not be permitted to adopt a new regulation regarding a fundamental statutory right like the statute of limitations and apply it retroactively. Far from being merely "procedural," statutes of limitations have the power to " 'alter the substantive rights of a party and increase a party's liability.' " *Hughes Aircraft Co.* v. *U.S. ex rel. Schumer*, 520 U.S. 939, 950 (1997) (quoting *Chenault* v. *U.S. Postal Service*, 37 F.3d 535, 537, 539 (9th Cir. 1994)). And in this case—as in the U.S.V.I. taxpayer cases discussed above—it was an abuse of the IRS's discretion to apply its 2010 regulation regarding the statute of limitations retroactively.

A. Because it implicates matters of fundamental fairness, the statute of limitations is not a mere procedural rule that can be changed without regard to its retroactive effect.

The IRS argues (at 42) that this Court should not even reach Home Concrete's retroactivity challenge, because the statute of limitations is merely a "procedural" rule of the sort that this Court "generally" applies to pending cases. But neither of the cases the IRS cites for this proposition goes as far as the IRS urges this Court to go. The IRS cites the dissent in *Lindh* v. *Murphy*, but fails to note that the *majority* held that the new standards in the Antiterrorism and Effective Death Penalty Act *did not* apply retroactively to the inmate's case. 521 U.S. 320, 322-23 (1997). And, although *Landgraf* v. *USI Film Products* noted that new procedural rules are often applied retroactively, *Landgraf*, like *Lindh*, declined to apply the 1991 amendments to Title VII (including at least one procedural amendment) retroactively. See *Landgraf*, 511 U.S. 244, 247, 275 (1994).

Further, as we have explained (*supra* at II.A), the statute of limitations is more than a mere "procedural" rule: it protects the fundamental value of fairness to U.S. taxpayers. This Court recognized as much when it quoted with approval a Ninth Circuit decision holding that " 'a newly enacted statute that lengthens the applicable statute of limitations may not be applied retroactively to revive a plaintiff's claim that was otherwise barred under the old statutory scheme[,] because to do so would alter the substantive rights of a party and increase a party's liability.' " *Hughes Aircraft Co.*, 520 U.S. at 950 (quoting *Chenault*, 37 F.3d at 537, 539). Thus, the IRS's argu-

ment that its new regulation interpreting the statute of limitations "is not retroactive in the relevant sense" simply will not wash. See IRS Br. at 40.

B. The IRS abused its discretion in applying the regulation in this case retroactively.

The IRS and Home Concrete also disagree about whether the IRS has authority to make the regulation at issue here retroactive in light of the 1996 Taxpayer Bill of Rights. See IRS Br. at 43; Home Concrete Br. at 46; see also Section 7805(b) (1995); Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1101(a), 110 Stat. 1452 (1996). But assuming *arguendo* that the IRS is correct and the Taxpayer Bill of Rights does not apply here, the IRS has still abused its discretion by applying this rule retroactively. *Gehl*, 795 F.2d at 1334. Even under the pre-1996 rules, the IRS "does not have carte blanche" to make all its regulations retroactive, and "the failure to limit a regulation to prospective application only" is reviewable for abuse of discretion. *Snap-Drape Inc.* v. *Comm'r*, 98 F.3d 194, 202 (5th Cir. 1996); see also *Auto. Club of Mich.* v. *Comm'r*, 353 U.S. 180, 184 (1957) (IRS's decision to apply rulings, regulations, or Treasury Decisions retroactively is reviewed for abuse of discretion).

Under settled precedent, "[a]n abuse of discretion may be found where the retroactive regulation alters settled prior law or policy upon which the taxpayer justifiably relied and if the change causes the taxpayer to suffer inordinate harm." *CWT Farms, Inc.* v. *Comm'r*, 755 F.2d 790, 802 (11th Cir. 1985); see *LeCroy Research Sys.*, 751 F. 2d at 127-28; *Gehl*, 795 F.2d at 1334; *Anderson, Clayton & Co.* v. *United States*, 562 F2d 972, 981 (5th Cir. 1977); *accord Cent.*

Ill. Pub. Serv. Co. v. *United States*, 435 U.S. 21, 38 (1978) (Powell, J., concurring) ("It seems particularly inappropriate for the Commissioner, absent express statutory authority, to impose retroactively a tax with respect to years prior to the date on which taxpayers are clearly put on notice of the liability.").

Here, the IRS's new regulation purports to "alter[]" over 40 years of law settled by this Court's holding in *Colony* interpreting the Section 6501(e) statute of limitations—an interpretation on which the taxpayers reasonably relied when they filed their 1999 tax returns. See Home Concrete Br. at 42-43. And the resulting harm is clear: the taxpayers are being forced to litigate their 1999 tax liability more than ten years later—a fate normally reserved for those who have failed to file returns at all, or who have filed false or fraudulent returns. *See* Section 6501(c)(1), (2), (3). Thus, the IRS abused its discretion when it made the 2010 regulation retroactively applicable to the taxpayers' case.

CONCLUSION

The taxpayers here have been put in the "all but intolerable" situation of standing ready "to produce vouchers, prove events, establish values and recall details of all that goes into an income tax contest" for over a decade. *Rothensies*, 329 U.S. at 301. That is exactly the result Congress sought to avoid when it passed Section 6501 and its predecessors. Under that statute, Congress has already given the IRS more than enough time to carry out its work. And, as the 2004 amendments show, Congress is ready and willing to give the IRS even more time as the need arises. What Congress has *not* given the IRS is the authority unilaterally to change the statute of limitations ap-

plicable to an entire category of taxpayers, and to apply its new rule retroactively.

In short, in its approach to the statute of limitations—in this case as in the U.S.V.I. taxpayer cases discussed above—the IRS is acting as a rogue agency. This Court should not tolerate the IRS's attempt to bypass the limits that Congress has placed on its authority. For that and the other reasons discussed in Respondents' brief, the judgment of the court of appeals should be affirmed.

Respectfully submitted.

VINCENT F. FRAZER
Attorney General
CAROL THOMAS-JACOBS
TAMIKA M. ARCHER
Assistant Attorneys General
Virgin Islands Department of Justice
GERS Complex
34-38 Kronprindsens Gade
St. Thomas, U.S.V.I. 00802
(340) 774-5666

GENE C. SCHAERR
Counsel of Record
LINDA T. COBERLY
PETER N. HIEBERT
BARRY J. HART
ADÈLE A. KEIM
Winston & Strawn LLP
1700 K Street, N.W.
Washington, DC 20006
(202) 282-5000
gschaerr@winston.com

Counsel for Amicus Curiae

DECEMBER 2011

ADDENDUM

Table 1: EXAMPLES OF FEDERAL TAX INCENTIVES IMPACTING STATE, LOCAL, TERRITORIAL, AND TRIBAL GOVERNMENTS SINCE 1986[1]

STATUTE	TAX INCENTIVE
Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, 107 Stat. 312	Tax Incentives for businesses in empowerment zones, enterprise communities, and rural development investment areas
	Accelerated depreciation for property on Indian reservations
	Indian employment credit
Small Business Job Protection Act of 1996, Pub. L. No. 104-188, 110 Stat. 1755	Deferral of gain on involuntary conversions resulting from Presidentially-declared disasters
	Exclusion of contributions in aid of construction for water and sewer utilities
	Deferral of tax on earnings of qualified State tuition programs

[1] Source: Joint Comm. on Taxation, 112th Cong., Background Information on Tax Expenditure Analysis and Historical Survey of Tax Expenditure Estimates at 26-35 (Feb. 28, 2011).

STATUTE	TAX INCENTIVE
Health Insurance Portability and Accountability Act of 1996, Pub. L. No. 104-191, 110 Stat. 1936	Tax incentives for D.C. Enterprise Zones
	D.C. first-time homebuyer tax credit
Community Renewal Tax Relief Act of 2000, incorporated by reference in the Consolidated Appropriations Act-FY 2001, Pub. L. No. 106-554, 114 Stat. 2763 (2000)	Renewal community tax incentives
	New markets tax credit
Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, 115 Stat. 38	Treatment of electing Alaska Native Settlement Trusts
Victims of Terrorism Tax Relief Act of 2001, Pub. L. No. 107-134, 115 Stat. 2427	Exclusion of survivor annuities paid to families of public safety officers killed in the line of duty

STATUTE	TAX INCENTIVE
Job Creation and Worker Assistance Act of 2002, Pub. L. 107-147, 116 Stat. 21	Additional first-year depreciation deduction for qualified New York Liberty Zone property
	Authority to issue $8 billion of tax-exempt private activity bonds to finance the construction and rehabilitation of nonresidential real property and residential rental real property in the New York Liberty Zone
	Authority for one additional advance refunding of certain bonds for facilities located in New York City
	Five-year recovery period for qualified New York Liberty Zone leasehold improvement property
American Jobs Creation Act of 2004, Pub. L. No. 108-357, 118 Stat. 1418	Exclusion of interest on State and local government bonds for qualified green building and sustainable design projects

STATUTE	TAX INCENTIVE
The Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users, Pub. L. No. 109-59, 119 Stat. 1144 (2005)	Exclusion of interest on State and local government qualified private activity bonds for highway projects and rail-truck transfer facilities
The Gulf Opportunity Zone Act of 2005, Pub. L. 109-135, 119 Stat. 2577	Additional first-year depreciation deduction for qualified Gulf Opportunity Zone property
	Ten-year carryback period for casualty losses of Gulf Opportunity Zone public utility property by reason of Hurricane Katrina
	Tax credit for the holders of Gulf Tax Credit Bonds
	Five-year carryback period for casualty losses of public utility property attributable to Hurricane Katrina

STATUTE	TAX INCENTIVE
The Tax Relief and Health Care Act of 2006, Pub. L. No. 109-432, 120 Stat. 2922	Tax credit for corporate income earned in American Somoa
Mortgage Forgiveness Debt Relief Act of 2007, Pub. L. No. 110-142, 121 Stat. 1803	Exclusion from gross income of benefits provided to local volunteer firefighters and emergency medical responders
Heroes Earnings Assistance and Relief Tax Act of 2008, Pub. L. No. 110-245, 122 Stat. 1624	Exclusion of certain State and local payments to military personnel
Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, 122 Stat. 2654	Additional standard deduction for State and local real property taxes

STATUTE	TAX INCENTIVE
Emergency Economic Stabilization Act of 2008, Energy Improvement and Extension Act of 2008, and Tax Extenders and Alternative Minimum Tax Relief Act of 2008, Pub. L. No. 110-343, 122 Stat. 3765	Tax exempt bond financing for the Midwestern Disaster Area
American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115	Deduction for any State or local sales or excise tax imposed on the purchase of a new car, light truck, motorcycle, or motor home
	Tribal economic development bonds
	Qualified school construction bonds
	Build America bonds that subsidize borrowing costs on taxable bonds incurred by State and local governments

AMICUS CURIAE BRIEF

No. 11-139

IN THE

Supreme Court of the United States

UNITED STATES OF AMERICA,
Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF OF AMERICAN COLLEGE OF TAX COUNSEL AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

RICHARD M. LIPTON
RUSSELL YOUNG
BAKER & MCKENZIE LLP
One Prudential Plaza
1300 East Randolph Dr.
Suite 3500
Chicago, IL 60601
(312) 861-7590

CLIFFORD M. SLOAN
Counsel of Record
PAMELA F. OLSON
JULIA M. KAZAKS
ARMANDO GOMEZ
DAVID W. FOSTER
MELISSA R. MIDDLETON
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
1440 New York Ave., NW
Washington, DC 20005
(202) 371-7000
cliff.sloan@skadden.com

Attorneys for Amicus Curiae

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

STATEMENT OF INTEREST 1

SUMMARY OF ARGUMENT 3

ARGUMENT 5

I. The Basis Regulation Operates Retroactively 5

II. Congress Has Generally Prohibited Treasury From Issuing Retroactive Regulations 8

A. *Section 7805(b) Generally Forbids Retroactive Regulations* 8

B. *The Current Version of Section 7805(b) Applies in This Case* 12

III. The Basis Regulation Is Impermissibly Retroactive Under *Landgraf* v. *USI Film Products* 18

IV. The Government's Interpretation of the Effective Date of the Regulation is Not Entitled to *Chevron* Deference 23

A. Mayo *Did Not Involve a Retroactive Regulation* 25

B. *Morton Involved a Newly-Enacted Statute That Specifically Authorized the Challenged Regulation* 27

V. Retroactivity Has an Adverse Effect on the Tax System 28

CONCLUSION 31

TABLE OF AUTHORITIES

CASES

American Trucking Ass'ns v. *Smith*,
496 U.S. 167 (1990) 22

Automobile Club of Michigan v. *Commissioner*,
353 U.S. 180 (1957) 11

Bell v. *Morrison*,
26 U.S. (1 Pet.) 351 (1828) 22

Boulware v. *United States*,
552 U.S. 421 (2008) 6

Bowen v. *Georgetown University Hospital*,
488 U.S. 204 (1988) ..... *passim*

Burks v. *United States*,
633 F.3d 347 (5th Cir. 2011), *petition for cert. pending*, 80 BNA U.S.L.W. 3090
(Aug. 11, 2011) (No. 11-178) 14, 23

Burlington Truck Lines, Inc. v. *United States*,
371 U.S. 156 (1962) 12

Chevron, U.S.A., Inc. v. *Natural Resources Defense Council, Inc.*,
467 U.S. 837 (1984) ..... *passim*

Chock Full O' Nuts Corp. v. *United States*,
453 F.2d 300 (2d Cir. 1971) 23

Colony Inc. v. *Commissioner*,
357 U.S. 28 (1958) 3, 6, 20

Eastern Enterprises v. *Apfel*,
524 U.S. 498 (1998) 19, 20

In re Enterprise Mortgage Acceptance Co., LLC, Securities Litigation,
391 F.3d 401 (2d Cir. 2004) 20, 22

Grapevine Imports, Ltd. v. *United States*,
636 F.3d 1368 (Fed. Cir. 2011), *petition for cert. pending*, 80 BNA U.S.L.W. 3090 (Aug. 5, 2011) (No. 11-163). 17

Guaranty Trust Co. v. *York*,
326 U.S. 99 (1945) 22

Home Concrete & Supply, LLC v. *United States*,
634 F.3d 249 (4th Cir. 2011) 27

Hughes Aircraft Co. v. *United States*,
520 U.S. 939 (1997)..... 20

Kandi v. *United States*,
No. C05-0840C, 2006 WL 834631
(W.D. Wash. Jan 11,2006)
aff'd in unpublished decision,
295 F. App'x 873 (9th Cir. 2008) 17

Landgraf v. *USI Film Products*,
511 U.S. 244 (1994) .....*passim*

Lindh v. *Murphy*,
521 U.S. 320 (1997) 21

Mayo Foundation for Medical Education & Research v. *United States*, 131 S. Ct. 704 (2011) ..... *passim*

Martin v. *Hadix*, 527 U.S. 343 (1999) 21

Murfam Farms v. *Commissioner*, 88 Fed. Cl. 516 (2009) 16, 17

Sala v. *United States*, 552 F. Supp. 2d 1167 (D. Colo. 2008), *rev'd on other grounds*, 613 F.3d 1249 (10th Cir. 2010) 17

Salman Ranch Ltd. v. *Commissioner*, 647 F.3d 929, (10th Cir. 2011), *petition for cert. pending*, 80 BNA U.S.L.W. 3322 (Nov. 7, 2011) (No. 11-583) 17

Schuman Aviation Co. v. *United States*, Civ. No. 08-289, 2011 U.S. Dist. LEXIS 100142 (D. Haw. Oct. 31, 2011) 11

Smiley v. *Citibank (South Dakota), N.A.*, 517 U.S. 735 (1996) 26

Stobie Creek Investments LLC v. *United States*, 82 Fed. Cl. 636 (2008), *aff'd on other grounds*, 608 F.3d 1366 (Fed. Cir. 2010), ... 17

Stogner v. *California*, 539 U.S. 607 (2003) 20

Sun Oil Co. v. *Wortman*,
486 U.S. 717 (1988) 22

Transpac Drilling Venture 1982-12 v. *Commissioner*,
147 F.3d 221 (2d Cir. 1998) 14

United Dominion Industries, Inc. v. *United States*,
532 U.S. 822 (2001) 26

United States v. *Mayo Foundation for Medical Education and Research*,
282 F. Supp. 2d 997 (D. Minn. 2003) 25

United States v. *Morton*,
467 U.S. 822 (1984) 24, 27, 28

United States v. *Zacks*, 375 U.S. 59 (1963) 7

Vons Cos. v. *United States*,
51 Fed. Cl. 1 (2001) 6

STATUTES AND REGULATIONS

26 U.S.C. § 752 ..... 16, 17

26 U.S.C. § 6229(d) 7

26 U.S.C. § 6501 ..... 6, 12, 18, 27

26 U.S.C. § 7805 (1994) 9

26 U.S.C. § 7805(b) ..... *passim*

Temp. Reg. § 301.6231(c)-5T 14

Treas. Reg. § 301.6501(e)-1 ..... *passim*

OTHER AUTHORITIES

138 Cong. Rec. S15356 (daily ed. Sept. 26, 1992) 16

American Jobs Creation Act of 2004, Pub. L. No. 108-357, 118 Stat. 1418 18

Benjamin J. Cohen & Catherine A. Harrington, *Is the Internal Revenue Service Bound by Its Own Regulations and Rulings?*, 51 Tax Law. 675 (1998) 16

General Counsel Memorandum ("GCM") 36856 (Sept. 21, 1976) 6

H. Rep. No. 506, 104th Cong., 2d Sess. (1996) ... 9, 15

I.R.M. 1.15.2.4 14

IRS Non Docketed Service Advice Review ("NSAR") 11419, 2000 WL 34423427 (July 10, 2000) 6

S. Rep. No. 169, 98th Cong., 2d Sess., 247 (1984) 14

Taxpayer Bill of Rights 2. Pub. L. No. 104-168, 110 Stat. 1452 (1996) 13, 15, 16

T.D. 9511, 2011-6 I.R.B. 455 ..... 5, 12

BRIEF OF AMERICAN COLLEGE OF TAX COUNSEL AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

American College of Tax Counsel (the "College") respectfully submits this brief as *amicus curiae* in support of respondents Home Concrete & Supply, LLC, et al.[1]

STATEMENT OF INTEREST

The College is a nonprofit professional association of tax lawyers in private practice, in law school teaching positions and in government, who are recognized for their excellence in tax practice and for their substantial contributions and commitment to the profession. The purposes of the College are:

- To foster and recognize the excellence of its members and to elevate standards in the practice of the profession of tax law;
- To stimulate development of skills and knowledge through participation in continuing legal education programs and seminars;

---

[1] Pursuant to Rule 37.6, counsel for *amicus curiae* states that no counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members, or its counsel made a monetary contribution to its preparation or submission. Petitioner and respondents have filed with the Clerk of the Court letters granting blanket consent to the filing of amicus briefs.

- To provide additional mechanisms for input by tax professionals in development of tax laws and policy; and
- To facilitate scholarly discussion and examination of tax policy issues.

The College is composed of approximately 700 Fellows chosen in recognition of their outstanding reputations and contributions in the field of tax law, and is governed by a Board of Regents consisting of one Regent from each federal judicial circuit, two Regents at large, the Officers of the College, and the last retiring Chair of the College.

This *amicus* brief is submitted by the College's Board of Regents and does not necessarily reflect the views of all members of the College, including those who are government employees.

The College submits this *amicus* brief because it is deeply troubled by the reliance of the taxing authorities in this case on a so-called retroactive "fighting regulation," which is a regulation issued to change the outcome of pending litigation in the government's favor. If the government is permitted to claim deference for such regulations, taxpayers will have little incentive to challenge wrongful government action because the government can overturn judicial decisions by issuing regulations while the decisions are awaiting rehearing or appellate review. Reliance on retroactive fighting regulations, and the claim that they should have retroactive effect and receive substantial deference, undermines the development of a tax system premised on predictability.

The College is aware that this case and several companion cases involve transactions that the government claims are "tax shelters." The College has repeatedly voiced its support for the government's efforts to curtail tax shelters. However, the need for powerful enforcement tools in the attack on tax shelters does not justify the issuance of retroactive fighting regulations, which are inconsistent with the highest traditions of the rule of law.

SUMMARY OF ARGUMENT

In *Mayo Foundation for Medical Education & Research* v. *United States*, 131 S. Ct. 704 (2011), this Court resolved a longstanding dispute between taxpayers and the government when it held that Treasury regulations, like regulations issued by other administrative agencies, should be evaluated under the framework set forth in *Chevron, U.S.A., Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984).

The authority that the government claims in this case, however, goes far beyond that which this Court approved in *Mayo*. This case does not involve a straightforward question of deference to a statutory interpretation with prospective effect; instead, it involves a claim of deference for a regulation issued with retroactive effect to revive claims that were barred by the statute of limitations. Previously, this Court's decision in *Colony Inc.* v. *Commissioner*, 357 U.S. 28 (1958), had been interpreted to apply a three-year statute of limitations to overstatements of basis. After several IRS assessments due to alleged basis overstatements were rejected by courts as

untimely, Treasury sought to have those decisions overturned on rehearing or on appeal by issuing a regulation that attempts to subject basis overstatements to a six-year statute of limitations. Moreover, Treasury is attempting to apply the new regulation, Treasury Regulation section 301.6501(e)-1(a)(1)(iii) (the "basis regulation"), with retroactive effect: Taxable years with respect to which the three-year statute had run before issuance of the regulation now would be reopened.

Retroactive "fighting" regulations like the basis regulation have two primary characteristics. First, they are issued by Treasury and the IRS to affect a "fight" with taxpayers, *i.e.*, to control the outcome of pending litigation. Second, the Treasury and the IRS claim that these regulations should have retroactive effect, *i.e.*, that they should change the tax consequences of closed transactions. Fighting regulations with retroactive effect should not be granted *Chevron* deference.

The retroactive fighting regulation in this case is especially problematic because it operates to revive claims that are otherwise barred under the applicable statute of limitations. Congress has made clear in section 7805(b) [2] that Treasury lacks authority to issue retroactive regulations except in limited circumstances that the government does not contend are present here. Moreover, the retroactive effect of the regulation also renders it impermissible

---

[2] Unless otherwise indicated, section references are to the Internal Revenue Code of 1986 (26 U.S.C. §§ 1 et seq. (the "Code")), as amended.

under *Landgraf* v. *USI Film Products*, 511 U.S. 244 (1994). Accordingly, it is not entitled to deference under *Chevron*.

This Court's jurisprudence should not be read to permit the government to circumvent section 7805(b) and to claim *Chevron*'s substantial deference for regulations issued to bootstrap the IRS's litigating position and reverse judicial decisions in which the IRS has been on the losing end. The Court's historic distrust of retroactive lawmaking should foreclose any reliance on retroactive fighting regulations, at least in the tax enforcement context. Permitting the government to resort to retroactive fighting regulations would have negative effects on the tax system. Fair and efficient tax administration requires that taxpayers be entitled to rely on the law, including Treasury regulations, as it exists at the time that they engage in transactions or file their returns.

ARGUMENT

I. The Basis Regulation Operates Retroactively.

In the preamble to the final basis regulation, Treasury stated that "these regulations are not retroactive."[3] Pet. App. 62a (T.D. 9511, 2011-6 I.R.B. 455, 456). Adhering to Treasury's preamble statement, the United States asserts in its opening brief that the basis regulation does not operate in a retroactive manner because it is simply a

---

[3] References to the Commissioner and the IRS include Treasury, where applicable.

restatement or clarification of existing law. (Brief for the United States ("CBr.") at 40-41.) The government's position lacks merit.

A simple example demonstrates that the regulation operates retroactively: A partnership and a partner filed the partnership and individual partner returns for the calendar year 2003 on April 15, 2004, and the IRS believes that the partner understated his gross income by more than 25% as a result of the partnership overstating its unrecovered cost or other basis. Prior to 2005, and at the time the taxpayer filed the return, the government had long considered *Colony Inc.* v. *Commissioner*, 357 U.S. 28 (1958), to be the governing law regarding section 6501. See IRS Non Docketed Service Advice Review ("NSAR") 11419, 2000 WL 34423427 (July 10, 2000) ("It has long been held that the extended statute of limitations provided in the case of a 25% omission is limited to when specific receipts or accruals are left out of the computation of gross income."); General Counsel Memorandum ("GCM") 36856 (Sept. 21, 1976) (*Colony* is "[t]he landmark case" interpreting section 6501(e), which the Court found to be "unambiguous").[4] The partner in the example would have expected the partnership to receive a Final Partnership Administrative

---

[4] Although neither NSARs nor GCMs are precedential under section 6110, this Court recently cited an NSAR as authority regarding the Commissioner's position in *Boulware* v. *United States*, 552 U.S. 421, 431 (2008); GCMs, moreover, "may be relevant . . . as indicating the IRS interpretation of its own regulations and procedures." *Vons Cos.* v. *United States*, 51 Fed. Cl. 1, 12 (2001).

Adjustment ("FPAA") within three years if the accuracy of the partnership return was contested (thereby giving him notice that items on his individual return may also be contested).[5] Thus, by April 16, 2007, if the IRS had not disputed the accuracy of the partnership return and issued an FPAA before that date, the partners could consider the partnership issues closed for 2003. See *United States* v. *Zacks*, 375 U.S. 59, 60 (1963) (explaining that the three year statute of limitations for filing refund claims "expired" three years after the taxpayers filed their returns; subsequent retroactive statutory change in the substantive law at issue could not revive taxpayer's time-barred claim for a refund). Under Treasury Regulation section 301.6501(e)-1, however, which became effective on September 24, 2009, the IRS would have had until January 1, 2010 to contest the partnership return. Thus, the regulation operates retroactively by permitting the IRS to reopen taxable years that were closed under the law that existed prior to the issuance of the regulation.

Here, the FPAA issued by the IRS in September 2006 was untimely under the law that existed when the taxpayers filed their returns in April 2000, when the three-year statute of limitations expired, and when the FPAA was issued. The new regulation, however, seeks to render timely the FPAA that was issued nearly six years after the return was filed based on a regulation that was not announced until

---

[5] The timely issuance of an FPAA suspends the running of the applicable assessment period for any individual partner. See 26 U.S.C. § 6229(d).

September 2009. This Court should not ignore the obvious fact that the regulation, "once effective, alter[s] the law applied in the past," *Bowen* v. *Georgetown Univ. Hosp.*, 488 U.S. 204, 217 (1988) (Scalia, J., concurring), merely because the Secretary has labeled the regulation as non-retroactive and provided it a then-current effective date.[6]

II. Congress Has Generally Prohibited Treasury From Issuing Retroactive Regulations.

A. *Section 7805(b) Generally Forbids Retroactive Regulations.*

In determining whether the regulation can be applied to reopen taxable years for which the statute of limitations has expired, the "threshold question is whether the [Internal Revenue Code] authorizes retroactive rulemaking." *Bowen*, 488 U.S. at 208. In addition to its erroneous argument that "[t]he regulation is not retroactive in the relevant sense" (CBr. 40), the government maintains that the "Treasury Department has express statutory authority to promulgate retroactive rules" (CBr. 42). In support of this argument, the government invokes

---

[6] There is impermissible retroactivity at issue here because the regulation "alter[s] the *past* legal consequences of past actions." *Bowen*, 488 U.S. at 219 (Scalia, J. concurring). This is not a situation where the regulation creates mere "'secondary' retroactivity," *i.e.*, where it is has "exclusively future effect" that "*affect[s]* past transactions," for example by "rendering the previously established [transactions] less desirable in the future." *Id.* at 219-220.

section 7805(b)(8) as the "relevant statute," but its argument rests on a misquotation of that provision.

Prior to July 1996, section 7805(b) stated that "[t]he Secretary may prescribe the extent, if any, to which any ruling or regulation, relating to the internal revenue laws, shall be applied without retroactive effect." 26 U.S.C. § 7805(b) (1994). The statutory language at that time, which granted the Secretary authority to issue regulations without retroactive effect, thus reflected an understanding that Treasury regulations generally could be applied retroactively. However, as part of the "Taxpayer Bill of Rights 2" in 1996, Congress amended the language of section 7805(b) to reflect its view that "it is generally inappropriate for Treasury to issue retroactive regulations." H. Rep. No. 506, 104th Cong., 2d Sess., 44 (1996).

Accordingly, the current version of the statute provides that:

> Except as otherwise provided in this subsection, no temporary, proposed, or final regulation relating to the internal revenue laws shall apply to any taxable period ending before the earliest of the following dates:
>
> (A) The date on which such regulation is filed with the Federal Register [;]
>
> (B) In the case of any final regulation, the date on which any proposed or temporary regulation to which such final regulation relates was filed with the Federal Register [;]

> (C) The date on which any notice substantially describing the expected contents of any temporary, proposed, or final regulation is issued to the public.

26 U.S.C. § 7805(b)(1)(A)-(C).

The statute then lists seven exceptions to its general prohibition on retroactive regulations. See 26 U.S.C. § 7805(b)(2)-(8). Without quoting the general prohibition on retroactive regulations in section 7805(b)(1), the government argues that one of these exceptions recognizes its authority to issue retroactive regulations such as the one at issue here: "The relevant statute, 26 U.S.C. 7805(b)(8), authorizes the Treasury Department to 'prescribe the extent, if any, to which any * * * regulation relating to the internal revenue laws shall be applied without retroactive effect.'" (CBr. 42.) But the government's use of the ellipsis deletes important statutory language.[7] The full text of section 7805(b)(8) actually provides: "The Secretary may prescribe the extent, if any, to which any ruling (including any judicial decision or any administrative determination other than by regulation) relating to the internal revenue laws shall be applied without retroactive effect." 26 U.S.C. § 7805(b)(8). The part of this provision the government submerges in ellipsis is crucial to its meaning.

---

[7] The government's quotation also fails to indicate the deletion of the closing parenthesis between "regulation" and "relating."

The full text shows that section 7805(b)(8) explicitly does not apply to *regulations*, much less recognize Treasury's authority to issue them retroactively. Instead, section 7805(b)(8) provides an explanation for how the new presumption against retroactivity applies to *rulings* (and notably is entitled "Application to Rulings"). See *Schuman Aviation Co.* v. *United States*, Civ. No. 08-289, 2011 U.S. Dist. LEXIS 100142 (D. Haw. Oct. 31, 2011) (finding that section "7805(b)(8) by its plain language, merely gives the IRS discretion to waive retroactive application of its rulings"). Section 7805(b)(8) specifically says that it applies to rulings, including administrative decisions "other than by regulation."[8]

Unlike the statute in *Bowen*, which authorized on its face some form of retroactive action by the agency, *Bowen*, 488 U.S. at 209, the government has not identified any provision in section 7805(b) or elsewhere in the Code that authorizes the government to issue the retroactive regulation at issue in this case. Instead, the government is faced with express language of Congress prohibiting this very type of regulation.

---

[8] *Automobile Club of Michigan* v. *Commissioner*, 353 U.S. 180 (1957), which the Commissioner also cites, was decided in 1957 and interpreted the pre-Taxpayer Bill of Rights 2 section 7805(b)—not current section 7805(b)(8), which does not apply to regulations. Thus, that case is not relevant to the interpretation of current section 7805(b)(8) as the government suggests.

B. *The Current Version of Section 7805(b) Applies in This Case.*

The position the government takes in its brief with respect to section 7805(b) is inconsistent with the position that Treasury took in promulgating the basis regulation. The government now admits that the current version of section 7805(b) is the "relevant statute," (CBr. at 42), for determining whether Treasury has the authority to promulgate retroactive regulations. But in the next paragraph of its brief, the government observes that Treasury rejected that position in adopting the basis regulation (*Id.* at 43 (quoting Pet. App. 62a-63a)). Instead, Treasury concluded in the preamble to the final basis regulation that, fifteen years after its enactment, the current version of section 7805(b) had yet to take effect with respect to regulations promulgated under section 6501(e) because section 6501 was first enacted before the Taxpayer Bill of Rights 2. See Pet. App. 62a-63a (T.D. 9511, 2011-6 I.R.B. 455, 456).

The government does not address the inconsistency between its current litigating position and its prior interpretation. Well-established principles of administrative law prohibit the government from taking new positions in litigation to justify administrative action that rested on a different position. See *Burlington Truck Lines, Inc.* v. *United States*, 371 U. S. 156, 168-169 (1962) ("The courts may not accept appellate counsel's post hoc rationalizations for agency action; [*SEC v.*] *Chenery* [*Corp.*, 332 U. S. 194 (1947),] requires that an agency's discretionary order be upheld, if at all, on

the same basis articulated in the order by the agency itself.").

The effective date of the current version of section 7805(b) is set forth in section 1101(a) of The Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1101(a), 110 Stat. 1452, 1469 (1996) and is entitled "Relief from Retroactive Application of Treasury Department Regulations." *Id.* at 1468. The effective date provision, which was not codified in the Code, states that the amendment "shall apply with respect to regulations which relate to statutory provisions enacted on or after the date of the enactment of this Act," (July 30, 1996). *Id.* at 1469.

The interpretive question is whether the phrase "enacted on or after the date of the enactment of this Act" should be read to modify "regulations" or "statutory provisions." The correct reading of this language is that the amendment applies to regulations that both (1) relate to statutory provisions and (2) were enacted on or after the Taxpayer Bill of Rights 2. The first requirement serves to make clear that the new general prohibition on retroactive regulations relates only to regulations that interpret the internal revenue laws and does not apply to regulations that pertain to internal Treasury Department policies, practices, and procedures. [9] The second requirement

---

[9] Similar language in other parts of section 7805 makes clear that Congress was aware that not all Treasury regulations interpret or relate to "Internal Revenue laws." See section 7805(b)(1) ("no temporary, proposed, or final regulation *relating to the internal revenue laws* shall apply to any taxable period ending *(cont'd)*

immediately implements Congress's judgment that retroactive regulations were improper for all regulations enacted after the Taxpayer Bill of Rights 2 went into effect.[10]

By contrast, Treasury's interpretation makes little sense in the context of the statute. Most of the sections of the Internal Revenue Code are longstanding and thus were enacted prior to July 30, 1996. Treasury's interpretation of section

---

(cont'd from previous page)
before the earliest of the following dates . . . ." (emphasis added)); section 7805(b)(5) ("The limitation in paragraph (1) shall not apply to any regulation relating to internal Treasury Department policies, practices, or procedures.").

[10] The law is clear that the word "enacted" is not limited to congressional action, and Courts and the IRS consider regulations to be "enacted." See I.R.M. 1.15.2.4 ("[s]pecific laws and regulations were enacted"); see also *Burks* v. *United States*, 633 F.3d 347, 350 & 360 n.9 (5th Cir. 2011) (referring to "recently enacted Treasury Regulations" and finding the government's allowance "for notice and comment after the final Regulations were enacted [was] not an acceptable substitute for prepromulgation notice and comment."), *petition for cert. pending*, 80 BNA U.S.L.W. 3090 (Aug 11, 2011) (No. 11-178); *Transpac Drilling Venture 1982-12* v. *Commissioner*, 147 F.3d 221, 225-226 (2d Cir. 1998) (citations omitted) ("[Respondent's argument] seeks to ground itself on Temporary Treasury Regulation § 301.6231(c)-5T ("Criminal Investigations Regulation"), which was enacted pursuant to TEFRA . . . ."); see also S. Rep. No. 169, 98th Cong., 2d Sess., 247 (1984) (referring to "Treasury regulations enacted following the Tax Reform Act of 1969").

7805(b)(1)'s effective date is that the new prohibition on retroactive regulations would apply only to the few sections that were enacted for the first time (not amended) after July 30, 1996. As discussed below, this interpretation of the effective date provision is contrary to the language of section 7805(b)(1), the purpose of the statute, the legislative history, at least four court cases, and the government's own arguments in other cases.

Had Congress meant to limit its retraction of the government's power such that section 7805(b)(1) would apply to almost no regulations, "this intent would have been made explicit," *Bowen*, 488 U.S. at 210, and not buried in an unclear effective date provision that could be read to undermine the entire amendment to the statute. The correct interpretation of the effective date provision is one that is consistent with Congress's stated intent to grant general "Relief from Retroactive Application of Treasury Department Regulations," The Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1101, 110 Stat. 1452, 1468 (1996), because "it is generally inappropriate for Treasury to issue retroactive regulations," H. Rep. No. 506, 104th Cong., 2d Sess., 44 (1996).

The legislative history indicates Congress's intent to issue a blanket prohibition against the issuance of retroactive regulations that relate to the internal revenue laws; Congress did not express an intention to narrow the scope of section 7805(b) such that it would apply only to regulations that deal with entirely new statutory provisions and not the bulk of the existing Internal Revenue Code. Instead, Congress intended to remove the government's

"stifling, awesome power . . . once and for all." 138 Cong. Rec. S15356 (daily ed. Sept. 26, 1992).[11]

Treasury's interpretation of the effective date is inconsistent with the government's position in two other cases. In *Murfam Farms* v. *United States*, 88 Fed. Cl. 516 (2009), the Court of Federal Claims applied the current version of section 7805(b) to a regulation that related to section 752, even though section 752 was originally enacted in 1954. Nowhere in the opinion was there a discussion of the purported narrow application of the effective date provision of section 7805(b). Instead, the current version of section 7805(b) was presumed to apply because the regulation at issue was issued after July 30, 1996. See *Murfam Farms*, 88 Fed. Cl. at 522-523. Notably, the government argued that the current version of section 7805(b) applied to the Code provision enacted in 1954, asserting that the

---

[11] Several bills prohibiting retroactive regulations passed Congress between 1988 and 1996, but were vetoed by the President on other grounds. The purposes of those bills, which carried over to the Taxpayer Bill of Rights 2 enacted in 1996, demonstrate Congress's intent to limit the Commissioner's ability to "change midstream the rules imposed on the American taxpayer," protecting against the Commissioner's "unfettered discretion" to apply the regulations retroactively, and preventing unfair "abuse of the use of promulgating and implementing retroactive regulations." 138 Cong. Rec. S15356 (daily ed. Sept. 26, 1992); see also Benjamin J. Cohen & Catherine A. Harrington, *Is the Internal Revenue Service Bound by Its Own Regulations and Rulings?*, 51 Tax Law. 675, 698-699 (1998) (describing legislative history of Taxpayer Bill of Rights 2).

"prevention of abuse" exception to the prohibition on retroactivity set forth in section 7805(b)(3) applied, but the Court held that the exception did not apply. *Id.* at 526-527.

In *Stobie Creek Investments LLC* v. *United States*, 82 Fed. Cl. 636, 668 (2008), *aff'd on other grounds*, 608 F.3d 1366 (Fed. Cir. 2010), the Court of Federal Claims also applied the current version of section 7805(b) to regulations that relate to section 752, even though section 752 was originally enacted in 1954. As in *Murfam*, the government argued that retroactive application of its regulations was permitted by the current version of section 7805(b)(3), but the Court held that exception did not apply. *Id.* at 668-670.

Other Courts also have applied the new version of section 7805(b) to regulations relating to statutory provisions that were enacted before July 1996. See *Cemco Investors, LLC* v. *United States*, 515 F.3d 749 (7th Cir. 2008) (applying current version of section 7805(b) to regulations relating to section 752, which was enacted prior to July 1996); *Sala* v. *United States*, 552 F. Supp. 2d 1167, 1197-1198 (D. Colo. 2008) (same), *rev'd on other grounds*, 613 F.3d 1249 (10th Cir. 2010) (no discussion of section 7805(b)); *Kandi* v. *United States*, No. C05-0840C, 2006 WL 83463 (W.D. Wash. Jan. 11, 2006) (applying current version of section 7805(b) to proposed regulations relating to section 7701, which was enacted prior to July 1996), *aff'd in unpublished decision*, 295 F. App'x 873 (9th Cir. 2008); but see *Salman Ranch Ltd.* v. *Commissioner*, 647 F.3d 929, 943 n.15 (10th Cir. 2011), *petition for cert. pending*, 80 BNA U.S.L.W. 3322 (Nov. 7, 2011) (No. 11-583); *Grapevine*

Imports, Ltd. v. *United States*, 636 F.3d 1368, 1381 n.6 (Fed. Cir. 2011), *petition for cert. pending*, 80 BNA U.S.L.W. 3090 (Aug. 5, 2011) (No. 11-163).[12]

At the very least, the effective date provision should be read to apply the current version of section 7805(b) to regulations that relate to statutory provisions that have been enacted, amended, or modified after July 30, 1996. Congress has enacted thirteen statutory provisions relating to section 6501 since 1996, at least one of which relates to section 6501(e)(1). See, *e.g.*, American Jobs Creation Act of 2004, Pub. L. No. 108-357, §§ 413(c)(28), 814(a), 118 Stat. 1418, 1509, 1581. Therefore, because section 6501 has been amended since July 30, 1996, the regulation at issue cannot operate retroactively under section 7805(b)(1).

III. The Basis Regulation Is Impermissibly Retroactive Under *Landgraf* v. *USI Film Products*.

Even if this Court were to conclude that Treasury retains some authority to issue retroactive regulations, the basis regulation nevertheless is impermissibly retroactive under this Court's decision in *Landgraf* v. *USI Film Products*, 511 U.S. 244 (1994). In *Landgraf*, this Court reaffirmed that "the presumption against retroactive legislation is deeply rooted in our jurisprudence." *Id.* at 265. In reaffirming this longstanding presumption, this

---

[12] In both *Salman* and *Grapevine*, however, the taxpayers did not contest the application of the older version of section 7805(b) and the courts addressed the effective date provision in footnotes only.

Court stated that the "principle that the legal effect of conduct should ordinarily be assessed under the law that existed when the conduct took place has timeless and universal appeal." *Id.* (citation omitted); see also *Eastern Enters.* v. *Apfel*, 524 U.S. 498, 532 (1998) (plurality op.) ("Retroactivity is generally disfavored in the law . . . ."); *id.* at 547 (Kennedy, J., concurring in the judgment and dissenting in part) ("[F]or centuries our law has harbored a singular distrust of retroactive statutes.").

Landgraf established a two-step test for judging applicability of a statute enacted after the events in the suit:

> [T]he court's first task is to determine whether Congress has expressly prescribed the statute's proper reach. If Congress has done so, of course, there is no need to resort to judicial default rules. When, however, the statute contains no such express command, the court must determine whether the new statute would have retroactive effect, *i.e.*, whether it would impair rights a party possessed when he acted, increase a party's liability for past conduct, or impose new duties with respect to transactions already completed. If the statute would operate retroactively, our traditional presumption teaches that it does not govern absent clear congressional intent favoring such a result.

Id. at 280.

Under *Landgraf*'s first step, there is no express congressional command because, after *Colony*, Congress never addressed extending the statute of limitations for basis overstatements from three years to six years. The general presumption against retroactivity thus applies to the basis regulation.

With respect to *Landgraf*'s second step—"whether the new [regulation] would have retroactive effect," 511 U.S. at 280—the regulation at issue here undeniably does: It purports to change the law governing returns filed a decade ago, thereby depriving taxpayers of an affirmative defense they possessed when they filed their returns and "increase[ing] [the taxpayer's] liability for past conduct"—an increase they would not have faced under pre-regulation law. *In re Enter. Mortg. Acceptance Co., LLC Sec. Litig.*, 391 F.3d 401, 409-410 (2d Cir. 2004) (quoting *Landgraf*, 511 U.S. at 280). This is impermissible "absent clear congressional intent favoring such a result." *Landgraf*, 511 U.S. at 280; see also *Hughes Aircraft Co.* v. *United States*, 520 U.S. 939, 950 (1997) ("extending a statute of limitations after the pre-existing period of limitations has expired impermissibly revives a moribund cause of action"); *Enter. Mortg.*, 391 F.3d at 407 ("a statute of limitations may not be applied retroactively to revive a claim that would otherwise be stale under the old scheme" (quoting *Chenault* v. *U.S. Postal Serv.*, 37 F.3d 535, 538 (9th Cir. 1994)); *id.* at 410 ("In our view, the resurrection of previously time barred claims has an impermissible retroactive effect."); see also *Stogner* v. *California*, 539 U.S. 607, 632 (2003)

(recognizing that California's extension of the statute of limitations for sex-related child abuse, where the prior limitations period had already expired, "retroactively [withdrew] a complete defense to prosecution after it ha[d] already attached" and thereby violated the Ex Post Facto Clause).

The government erroneously argues that the "regulation is not retroactive in the relevant sense" (CBr. at 40), and in defense of that position, the government argues that the regulation is procedural and "does not bear on the legality of the petitioners' conduct" (CBr. at 41). But this observation about the regulation does not cure its impermissibly retroactive effect, and it is in any event unsupported by the authority the government cites. The government quotes *Lindh* v. *Murphy*, 521 U.S. 320, 341 (1997) (CBr. at 42), in support of its argument, but it does not note that the language it quotes comes from Chief Justice Rehnquist's dissenting opinion, not from the Court's opinion. Moreover, this Court has cited its majority decision in *Lindh* as evidence of its painstaking effort "to dispel the 'suggestion that concerns about retroactivity have no application to procedural rules.'" *Martin* v. *Hadix*, 527 U.S. 343, 359 (1999) (citing *Landgraf*, 511 U.S. at 275; *Lindh*, 521 U.S. at 327-328) (alteration omitted). Thus, *Lindh* simply does not stand for the proposition for which the government cites it.

"When determining whether a new statute operates retroactively, it is not enough to attach a label (*e.g.*, 'procedural,' 'collateral') to the statute; [a court] must ask whether the statute operates retroactively." *Martin*, 527 U.S. at 359. Statutes of limitations "protect interests in reliance and repose,"

Am. Trucking Ass'ns v. *Smith*, 496 U.S. 167, 214 (1990), guard "against stale demands," *Bell* v. *Morrison*, 26 U.S. (1 Pet.) 351, 360 (1828), and limit the circumstances in which a reviewing court can grant relief, *In re Enter. Mortg. Acceptance Co., LLC Sec. Litig.*, 391 F.3d 401, 409 (2d Cir. 2004). "Because, in different contexts, a statute of limitations may fairly be described as either procedural or substantive," *id.*, this Court should decline the government's invitation to designate all statutes of limitations "procedural" and thereby sanction a revision to a statute of limitations that operates retroactively to re-open taxable years that previously were closed under existing law.[13]

---

[13] "[S]tatutes of limitations . . . are rationally capable of classification as either procedural or substantive." *Enter. Mortg.*, 391 F.3d at 409 n.6 (alteration in original) (quoting Fleming James, Jr., Geoffrey C. Hazard, Jr. & John Leubsdorf, *Civil Procedure* § 2.37, at 130-31 (4th ed. 1992)); *see also Sun Oil Co.* v. *Wortman*, 486 U.S. 717, 722-29 (1988) (holding that statutes of limitations were properly treated as "procedural" for choice-of-law purposes in context of Full Faith and Credit Clause while noting that *Guaranty Trust Co.* v. *York*, 326 U.S. 99 (1945), treated statutes of limitations as "substantive" for *Erie* doctrine purposes); *Wortman*, 486 U.S. at 727 ("[T]he words 'substantive' and 'procedural' themselves . . . do not have a precise content, even (indeed especially) as their usage has evolved.").

IV. The Government's Interpretation of the Effective Date of the Regulation Is Not Entitled to *Chevron* Deference.

The government candidly concedes that it enacted the regulation in this case to "reverse [the] judicial decisions" in which the government was the losing party. (CBr. 40.) It also asserts that, despite this litigation-strategy posture, *Chevron* deference should be given to the regulation in this case (and others pending) in which the three-year statute of limitations expired before issuance of the FPAA. This Court should not permit the government to claim deference for a regulation issued with retroactive effect to overturn its litigation losses in pending cases.

This Court has held that "[d]eference to what appears to be nothing more than an agency's convenient litigating position" is "entirely inappropriate." *Bowen*, 488 U.S. at 213; see also *Burks*, 633 F.3d at 360 n.9 (finding that even if the statute were not unambiguous, it is "unclear whether the Regulations would be entitled to *Chevron* deference under *Mayo*" because "in *Mayo* the Supreme Court was not faced with a situation where, during the pendency of the suit, the treasury promulgated determinative, retroactive regulations following prior adverse judicial decisions on the identical legal issue"); *Chock Full O' Nuts Corp.* v. *United States*, 453 F.2d 300, 303 (2d Cir. 1971) ("[T]he Commissioner may not take advantage of his power to promulgate retroactive regulations during the course of a litigation for the purpose of providing himself with a defense based on the presumption of validity accorded to such regulations.").

There are strong reasons for this Court to reject Treasury's attempt to bootstrap the IRS litigating position through regulations. As an initial matter, permitting the government to overturn its litigation losses in pending cases by issuing retroactive regulations discourages taxpayers from bringing meritorious challenges to unlawful IRS or Treasury action. There is little reason to challenge the government if it can simply rewrite the rules retroactively when it is losing. Moreover, deference in these circumstances discourages the IRS from devoting resources to conducting efficient, timely audits, and it instead encourages the IRS to rely on retroactive regulations to remedy its tax administration failures. Finally, when Treasury and the IRS adopt retroactive fighting regulations, there is reason to believe that the regulations are prompted by the government's distaste for losing as much as by its expert administrative judgment that the law should be clarified or altered. For these reasons, *Chevron* deference is not appropriate for retroactive fighting regulations.

To defeat application of *Landgraf*, *Bowen*, and current section 7805(b)(1), the government relies on this Court's decisions in *Mayo Foundation for Medical Education & Research* v. *United States*, 131 S. Ct. 704 (2011) and *United States* v. *Morton*, 467 U.S. 822 (1984). As explained below, those cases do not grant the government the authority that it claims.

A. Mayo *Did Not Involve a Retroactive Regulation.*

In *Mayo*, this Court stated that it is "immaterial to [its] analysis that a 'regulation was prompted by litigation.'" *Mayo*, 131 S. Ct. 704, 712 (2011) (citation omitted). In so stating, this Court was not faced with a regulation that operated to undo a multitude of cases that had already been litigated at both the trial and appellate levels because the regulation at issue in *Mayo* notably *did not* operate retroactively. Because the regulation at issue in *Mayo* was not retroactive, this Court's decision to defer to the regulation did not operate to reverse the outcome of *United States* v. *Mayo Foundation for Medical Education and Research*, 282 F. Supp. 2d 997 (D. Minn. 2003), which prompted the government to issue the regulation in 2004 after it lost that case in 2003. The regulation at issue here goes beyond what this Court addressed in *Mayo*—this regulation was not just "prompted" by litigation, it was issued with the stated purpose of *reversing* judicial decisions, and not just in the sense of changing the outcome of future cases by setting favorable precedent, but with the stated purpose of reversing decisions in which the government was the losing party. *Mayo* thus did not present this Court with an opportunity to consider the interaction between its prior decisions disfavoring retroactive lawmaking, see, *e.g.*, *Landgraf* and *Bowen*, and its decision in *Chevron* (in addition to addressing the change in law of section 7805(b)).

Unlike here, in *Mayo*, the government lost a decision in 2003 and amended the regulation to change the law on a *prospective basis only*, leaving

undisturbed the result reached by the district court in 2003 for the 1994-1996 tax years. The government did not try to "reverse" a court decision that it lost. The government's actions in *Mayo* are consistent with the prohibition on retroactive regulations found in section 7805(b)(1).[14]

In *Mayo*, this Court noted that it has in the past invited the Treasury Department to amend its regulations if it is "troubled by the consequences of [the Court's] resolution of the case." *Mayo*, 131 S. Ct. at 712-713 (citing *United Dominion Industries, Inc.* v. *United States*, 532 U.S. 822, 838 (2001)). Notably, the Court in *Dominion Industries* did not invite the Treasury Department to reverse the Court's very decision by issuing a retroactive regulation *to undo that decision*—instead, this Court's invitation can properly be viewed as an invitation to change the law on a prospective basis. Limiting Treasury's power to change the law on a prospective basis except in limited circumstances is

---

[14] This Court's decision in *Smiley* v. *Citibank (South Dakota), N.A.*, 517 U.S. 735 (1996), also addressed regulations that were prompted by litigation. However, the banking regulation at issue in *Smiley* was not retroactive, did not change the outcome of the litigation that prompted it, and was not issued by a party to that litigation (The Comptroller of the Currency was *amicus curiae* in the litigation prompting the subsequent issuance of the regulation). Both the majority opinion and the concurrence in *Bowen* suggest that, if the regulation in *Smiley* had the characteristics of the regulation at issue here, this Court might have reached a different result regarding the deference point.

proper because "agencies are not a law unto themselves. No less than any other organ of government, they operate in a system in which the last words in law belong to Congress and the Supreme Court." *Home Concrete & Supply, LLC* v. *United States*, 634 F.3d 249, 259 (4th Cir. 2011) (Wilkinson, J., concurring).

B. Morton *Involved a Newly-Enacted Statute that Specifically Authorized the Challenged Regulation.*

In *Morton*, this Court stated in a footnote that the regulation was permissible even if it was issued in response to litigation because Congress had specifically authorized the agency to issue regulations to interpret the newly enacted statute to which the regulation related. *Morton*, 467 U.S. at 836 n.21. That is not the case here. Section 6501 is not newly enacted and does not contain a specific grant of authority for Treasury to issue regulations relating to that section. The regulation at issue here was issued pursuant to Treasury's general regulatory authority under section 7805(a). More importantly, unlike in *Morton* where Congress sought to have administrative problems of the type at issue in that litigation addressed by the agency through regulations, Congress has *expressly prohibited* Treasury from issuing retroactive regulations such as the ones at issue here.

If section 6501 were a newly enacted statute as was the case in *Morton*, then Treasury would have been authorized to issue retroactive regulations dating back to the date of enactment of the statute pursuant to section 7805(b)(2)—the exception for

"promptly issued regulations." That exception does not apply here, however, because Treasury was not completing "the task which Congress ha[d] assigned it." *Morton*, 467 U.S. at 836 n.21.

Treasury lacks authority to issue retroactive regulations given the express language in section 7805(b)(1) and the clear legislative history further evidencing Congress's intent to ban this practice once and for all. As a result, its regulation is not entitled to deference.

V. Retroactivity Has an Adverse Effect on the Tax System.

The College supports the IRS' efforts to challenge "tax shelter" transactions that have the effect of reducing tax liability in a manner unintended by Congress. The College recognizes that taxpayers' success in avoiding their tax liabilities can have a corrosive effect on the tax system. The College further recognizes that the government promulgated the basis regulation as part of its effort to curtail what it views as inappropriate tax avoidance. That said, ends do not always justify means. While the College believes it is critical for the proper functioning of the tax system that the IRS prevent inappropriate tax avoidance, it also believes that the issuance of retroactive fighting regulations to change the outcome of pending litigation is inherently unfair, is inconsistent with the highest traditions of the rule of law, and will undermine support for the tax system.

The prohibition against retroactive regulations is derived from the sound tax policy that taxpayers are entitled to rely on the law, including Treasury

regulations, as it exists at the time they engage in transactions or file their tax returns. Looking in particular at the policy of the statute of limitations, Congress decided that it was not in the best interests of the tax system to have tax cases begun more than three years after returns are filed, with all of the attendant issues relating to recordkeeping and reconstruction of transactions, subject only to an exception if the taxpayer's return omits substantial gross income and therefore justifies an extension of the otherwise applicable statute of limitations. The statute of limitations also has the beneficial effect of encouraging the IRS to conduct timely, efficient audits of taxpayers' returns.

In promulgating retroactive regulations to support ongoing litigation, the government sends the wrong message to the taxpaying public. In order for a self-reporting tax system such as ours to function properly, taxpayers must have confidence in the fairness and efficiency of the system and its administration. Fair and efficient tax administration, in turn, requires that taxpayers be able to rely on the law as it exists at the time that they engage in transactions and file their tax returns. Statutes of limitations are an important aspect of tax administration, and all taxpayers should be allowed to rely on them, regardless of one's view of the propriety of the result occasioned by the expiration of the limitations period.[15]

---

[15] Although the subject of this case is the retroactive application of the basis regulation to a transaction that the IRS contends is a "tax shelter," the government *(cont'd)*

As a general matter, the College long has supported the government's effort to combat "tax shelters" and otherwise curtail inappropriate tax avoidance. But as laudable as the government's goal may be, the important principles of fairness and predictability underlying the strong public policy against retroactivity prevent the government from using retroactive fighting regulations to administer the tax system.

(cont'd from previous page)
acknowledges that the basis regulation applies to situations that do not involve tax shelters. Pet. for Cert. Reply Brief at 4.

CONCLUSION

For the foregoing reasons, this Court should not accord deference to the basis regulation, Treas. Reg. section 301.6501(e)-1(a)(1)(iii).

Respectfully submitted,

RICHARD M. LIPTON
RUSSELL YOUNG
BAKER & MCKENZIE LLP
One Prudential Plaza
1300 East Randolph Dr.
Suite 3500
Chicago, IL 60601
(312) 861-7590

CLIFFORD M. SLOAN
Counsel of Record
PAMELA F. OLSON
JULIA M. KAZAKS
ARMANDO GOMEZ
DAVID W. FOSTER
MELISSA R. MIDDLETON
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
1440 New York Ave., NW
Washington, DC 20005
(202) 371-7000
cliff.sloan@skadden.com

Attorneys for Amicus Curiae

December 22, 2011

AMICUS CURIAE BRIEF

No. 11-139

IN THE

Supreme Court of the United States

UNITED STATES,
Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF OF *AMICUS CURIAE* BAUSCH & LOMB INCORPORATED IN SUPPORT OF RESPONDENTS

LISA S. BLATT
Counsel of Record
ANTHONY J. FRANZE
R. STANTON JONES
ARNOLD & PORTER LLP
555 12th Street, N.W.
Washington, DC 20004
(202) 942-5000
lisa.blatt@aporter.com

Counsel for Amicus Curiae Bausch & Lomb Incorporated

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
INTEREST OF *AMICUS CURIAE*	1
INTRODUCTION AND SUMMARY OF ARGUMENT	4
ARGUMENT	7
I. REGARDLESS OF HOW THE COURT INTERPRETS SECTION 6501(e)(1)(A), THE TAXPAYER WOULD PREVAIL UNDER SECTION 6229(c)(2)	7
A. Sections 6501(e)(1)(A) and 6229(c)(2) Extend the Limitations Period for Tax Assessments in Different Circumstances	8
B. *Colony* Controls the Meaning of Section 6229(c)(2)	13
II. THE GOVERNMENT'S POSITION WOULD APPLY TO LEGITIMATE BUSINESS TRANSACTIONS; AND IT IS UNNECESSARY TO COMBAT ABUSIVE TAX SHELTERS	21
CONCLUSION	27

TABLE OF AUTHORITIES

CASES	Page(s)
Bragdon v. Abbott, 524 U.S. 624 (1998)	14
Burks v. United States, 633 F.3d 347 (5th Cir. 2011), *petition for cert. filed* (U.S. Aug. 11, 2011) (No. 11-178)	3
Cannon v. Univ. of Chicago, 441 U.S. 677 (1979)	13
Chase Sec. Corp. v. Donaldson, 325 U.S. 304 (1945)	6, 21
Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837 (1984)	15, 17
Colony, Inc. v. Comm'r, 357 U.S. 28 (1958)	*passim*
Conroy v. Aniskoff, 507 U.S. 511 (1993)	13
Corley v. United States, 129 S. Ct. 1558 (2009)	13
Curr-Spec Partners, L.P. v. Comm'r, 579 F.3d 391 (5th Cir. 2009)	10
Grapevine Imports, Ltd. v. United States, 636 F.3d 1368 (Fed. Cir. 2011) *petition for cert. filed* (U.S. Aug. 5, 2011) (No. 11-163)	4
Home Concrete & Supply, LLC v. United States, 634 F.3d 249 (4th Cir. 2011)	3, 10
In re Becker, 407 F.3d 89 (2d Cir. 2005)	22

TABLE OF AUTHORITIES—Continued

Page(s)

Intermountain Ins. Serv. of Vail, LLC v. Comm'r, 650 F.3d 691 (D.C. Cir. 2011), *petition for cert. filed* (U.S. Nov. 16, 2011) (No. 11-663) 2, 4, 18, 22

Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA, 130 S. Ct. 1605 (2010) 14

Lindh v. Murphy, 521 U.S. 320 (1997) 19

Lorillard v. Pons, 434 U.S. 575 (1978) 13

Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 545 U.S. 967 (2005) 17, 18

Plaut v. Spendthrift Farm, Inc., 514 U.S. 211 (1995) 21-22

Reynolds Props., L.P. v. Comm'r, Nos. 10-72406, 10-73376 (9th Cir. argued Oct. 13, 2011) 3

Rhone-Poulenc Surfactants & Specialties L.P. v. Comm'r, 114 T.C. 533 (2000) 9

Russello v. United States, 464 U.S. 16 (1983) 18

Salman Ranch, Ltd. v. Comm'r, 647 F.3d 929 (10th Cir. 2011), *petition for cert. filed* (U.S. Nov. 7, 2011) (No. 11-582) 3

UTAM, Ltd. v. Comm'r, 645 F.3d 415 (D.C. Cir. 2011), *petition for cert. filed* (U.S. Dec. 14, 2011) (No. 11-747) 3-4

TABLE OF AUTHORITIES—Continued

Page(s)

Wilmington Partners L.P. v. Comm'r, No. 10-4183 (2d Cir. argued Aug. 26, 2011) 2, 10, 23

STATUTES AND REGULATORY PROVISIONS

26 U.S.C. ch. 63, subch. C 9

26 U.S.C. ch. 66 8

26 U.S.C. § 275(c) (1940) ..... *passim*

26 U.S.C. § 701 ..... 8, 9

26 U.S.C. § 702 9

26 U.S.C. § 703 9

26 U.S.C. § 704 9

26 U.S.C. § 6011 24

26 U.S.C. § 6031 8

26 U.S.C. § 6229 (2000) ..... *passim*

26 U.S.C. § 6229(a) (2000) 9

26 U.S.C. § 6229(c)(1) 24

26 U.S.C. § 6229(c)(2) (2000) ..... *passim*

26 U.S.C. § 6231(a)(3) 8-9

26 U.S.C. § 6501 (2000) ..... *passim*

26 U.S.C. § 6501(a) (2000) 8

26 U.S.C. § 6501(c)(1) 24

26 U.S.C. § 6501(c)(2) 24

26 U.S.C. § 6501(c)(10) 6, 21, 23, 24

26 U.S.C. § 6501(e) (2000) 5, 14, 18

TABLE OF AUTHORITIES—Continued

Page(s)

26 U.S.C. § 6501(e)(1)(A) (2000) ..... *passim*

26 U.S.C. § 6501(e)(1)(A)(i) (2000) ..... *passim*

26 U.S.C. § 6501(e)(1)(B)(i) 12

26 U.S.C. § 6501(e)(1)(B)(ii) 12

26 U.S.C. § 6501(e)(2) (2000) 15, 16, 17, 19

26 U.S.C. § 6501(n)(2) 19

26 U.S.C. § 6707A(c)(2) 23

American Jobs Creation Act of 2004, Pub. L. No. 108-357, 118 Stat. 1418 ..... 21, 23

Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, 124 Stat. 71 (2010) 12

Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, 96 Stat. 324 11

Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2085 14

Technical and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, 102 Stat. 3342 14

Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788 14

Temp. Treas. Reg. § 301.6229(c)(2)-1T(a) (2009) 7, 13

Temp. Treas. Reg. § 301.6501(e)-1T(a) (2009) 7, 12

T.D. 9466, 2009-43 I.R.B. 551, *reprinted in* 74 Fed. Reg. 49,321 (Sept. 28, 2009) ..... *passim*

TABLE OF AUTHORITIES—Continued

Page(s)

T.D. 9511, 2011-1 C.B. 455, *reprinted in* 75 Fed. Reg. 78,897 (Dec. 17, 2010) 12

Treas. Reg. § 301.6229(c)(2)-1(a) (2010) 7, 13

Treas. Reg. § 301.6501(e)-1(a) (2010) 7, 12

OTHER AUTHORITIES

Joshua D. Blank, *What's Wrong with Shaming Corporate Tax Abuse*, 62 Tax L. Rev. 539 (2009) 24

Brief for United States, *United States v. Brockamp*, 519 U.S. 347 (1997) (No. 95-1225) 25

I.R.S. F.S.A. 1591, 1995 FSA LEXIS 354 (May 10, 1995) 19

I.R.S. Gen. Counsel Mem. 36,856 (Sept. 21 1976) 14

Elliot Pisem & Jason K. Binder, Blak *Affirms the Necessity of Raising S/L Defenses Early in TEFRA Partnership Proceedings*, 112 J. Tax'n 222 (2010) 24

IN THE

Supreme Court of the United States

No. 11-139

UNITED STATES,

Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, *et al.*,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF OF *AMICUS CURIAE* BAUSCH & LOMB INCORPORATED IN SUPPORT OF RESPONDENTS

INTEREST OF *AMICUS CURIAE*[1]

Bausch & Lomb Incorporated ("B&L") is an eye health company. Founded in 1853, it is one of the oldest, best known, and most respected healthcare

[1] No counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of this brief. No one other than *amicus curiae* or its counsel made a monetary contribution to the preparation or submission of this brief. Letters from the parties consenting to the filing of this brief have been filed with the Clerk of the Court.

brands in the world. B&L has a substantial financial interest in the resolution of this case and a unique perspective on the potential breadth of the government's arguments.

B&L has a related case pending in the Second Circuit where the IRS seeks to assess taxes in an amount that exceeds the *combined* amount at issue in *all* of the cases cited in the government's brief involving Son-of-BOSS tax shelters. *See Wilmington Partners L.P. v. Comm'r*, No. 10-4183 (2d Cir. argued Aug. 26, 2011). While the government's brief in the present case invokes the need to combat those tax shelters, B&L's case involves neither a Son-of-BOSS transaction nor an abusive tax evasion scheme. *See Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 650 F.3d 691, 699 (D.C. Cir. 2011) (recognizing that B&L's case involves "no Son of Boss tax shelter allegation"), *petition for cert. filed* (U.S. Nov. 16, 2011) (No. 11-663); U.S. Cert. Reply at 4 (similar).

If the taxpayer prevails here, B&L will prevail in the Second Circuit. The case before the Court presents the question of whether under 26 U.S.C. § 6501(e)(1)(A) (2000) an overstatement of basis on a tax return constitutes an omission from the *taxpayer's* gross income, giving the IRS an extended six-year limitations period to assess any tax. B&L's case presents the same question under 26 U.S.C. § 6229(c)(2) (2000) with respect to partnerships, *i.e.*, whether an overstatement of basis is an omission from the *partnership's* gross income, triggering an extended six-year limitations period for an IRS assessment.

In B&L's case, the IRS seeks to assess hundreds of millions of dollars in taxes, penalties, and interest against B&L based on an alleged $550 million overstatement of basis on a partnership's return. The IRS relies on Section 6229(c)(2) to extend the limitations period to six years because the IRS failed to assess any tax or give notice of an assessment within three years after the partnership's return was filed. Although B&L's case involves Section 6229(c)(2) and not 6501(e)(1)(A), B&L has a direct interest in the case before the Court because the IRS erroneously equates the two statutes in arguing that an overstatement of basis is an omission from gross income.

B&L's case also underscores the far-reaching and adverse implications of the government's position. The government advocates a lenient limitations period purportedly based on the need to combat "manipulati[ve]" tax evasion schemes. U.S. Br. 11-12. But B&L's case does not involve such a transaction. To the contrary, B&L's case arises from the IRS's inexplicable delay in examining the tax consequences of a series of legitimate business transactions.

B&L has a long history and informed perspective on the questions before the Court. B&L has filed *amicus* briefs in six circuits in cases involving both Sections 6501 and 6229.[2] The government has

---

[2] *See Home Concrete & Supply, LLC v. United States*, 634 F.3d 249 (4th Cir. 2011); *Burks v. United States*, 633 F.3d 347 (5th Cir. 2011), *petition for cert. filed* (U.S. Aug. 11, 2011) (No. 11-178); *Reynolds Props., L.P. v. Comm'r*, Nos. 10-72406, 10-73376 (9th Cir. argued Oct. 13, 2011); *Salman Ranch, Ltd. v. Comm'r*, 647 F.3d 929 (10th Cir. 2011), *petition for cert. filed* (U.S. Nov. 7, 2011) (No. 11-582); *UTAM, Ltd. v. Comm'r*, 645

acknowledged B&L's history with the issues before this Court. *See* U.S. Br. 29, 39. And B&L filed an *amicus* brief at the certiorari stage in this case.

INTRODUCTION AND SUMMARY OF ARGUMENT

I. The tax liability asserted in B&L's pending case in the Second Circuit dwarfs the asserted liability in this case. Whereas this case involves an alleged $6 million overstatement of basis, Pet. App. 28a-29a, B&L's case involves an alleged *half billion* dollar overstatement of basis and, according to the government, more than that amount in taxes, penalties, and interest. Indeed, the IRS erroneously seeks to extend the limitations period to assess an amount against B&L that exceeds the *combined* amount at stake in *all* of the Son-of-BOSS tax shelter cases discussed in the government's merits brief. And B&L's case does not involve an alleged abusive tax shelter.

Although B&L's case involves the different statute of limitations under 26 U.S.C. § 6229(c)(2) (2000) and not Section 6501(e)(1)(A), the IRS erroneously equates the two statutes in seeking to expand the statute of limitations set by Congress for omissions from gross income. Accordingly, the IRS in B&L's case makes the same arguments as those presented here and similarly attempts to invoke a regulation that the IRS promulgated to overturn its losses in litigation.

F.3d 415 (D.C. Cir. 2011), *petition for cert. filed* (U.S. Dec. 14, 2011) (No. 11-747); *Intermountain*, 650 F.3d 691 (D.C. Cir. 2011); *Grapevine Imports, Ltd. v. United States*, 636 F.3d 1368 (Fed. Cir. 2011), *petition for cert. filed* (U.S. Aug. 5, 2011) (No. 11-163).

B&L fully agrees with respondents that an overstatement of basis is not an omission from the taxpayer's gross income under Section 6501(e)(1)(A). *See* Resp. Br. 22-36. B&L also agrees that the IRS regulations on their face do not open settled tax years and, in any event, are invalid. *See id.* at 36-50. But regardless of the outcome under Section 6501(e)(1)(A), the statutory text, structure, and history of Section 6229(c)(2) confirm that an overstatement of basis is not an omission from a partnership's gross income.

Section 6229(c)(2) contains *exactly the same* statutory language that this Court construed in *Colony, Inc. v. Commissioner*, 357 U.S. 28 (1958). *Colony* held that an overstatement of basis is not an omission from gross income within the meaning of former Section 275(c). Congress enacted Section 6229(c)(2) in 1982, nearly a quarter century after *Colony* and against the backdrop of that decision. In light of Congress's reenactment of the same statutory language, *Colony* controls the meaning of Section 6229(c)(2).

Further, Section 6229 does not contain either of the "adjacent provisions" from Section 6501(e) on which the government places all but dispositive weight to overrule *Colony* as applied to Section 6501(e)(1)(A). U.S. Br. 20-24. B&L agrees with respondents that the government's reliance on those adjacent provisions is seriously misplaced. *See* Resp. Br. 30-33, 35 n.14. But the more the government relies on the provisions, the more the government's arguments demonstrate that the taxpayer would prevail under Section 6229(c)(2). At a minimum, if the government prevails in this case, the Court's opinion should make clear that the interpretation of Section

6501(e)(1)(A) does not control the meaning of Section 6229(c)(2).

II. The government's policy arguments with respect to both Sections 6501(e)(1)(A) and 6229(c)(2) also are fundamentally unsound. The government advocates an expansive view of the limitations period for tax assessments purportedly based on the need to combat "manipulati[ve]" "tax-avoidance schemes." U.S. Br. 11-12, 25. Limitations periods, however, "are by definition arbitrary, and their operation does not discriminate between the just and the unjust claim." *Chase Sec. Corp. v. Donaldson*, 325 U.S. 304, 314 (1945).

The general limitations periods under Sections 6501 and 6229 apply to abusive tax evasion schemes and legitimate business transactions alike. B&L's pending case reflects that the government's position could unjustifiably excuse the government's dilatory conduct for countless good faith disputes over legitimate business transactions.

In any event, in 2004 Congress amended the Tax Code and effectively gave the IRS an open-ended statute of limitations for abusive tax shelters or so-called "listed transactions." 26 U.S.C. § 6501(c)(10). The government's theory therefore would serve only to excuse the IRS's belated assessments in cases, such as B&L's, involving transactions that are not listed tax shelters. Indeed, citing B&L's case, the government at the certiorari stage advised the Court that the issues in this case can "arise in cases that do not involve Son-of-BOSS shelters or any other type of 'listed transaction.'" U.S. Cert. Reply at 4.

ARGUMENT

I. REGARDLESS OF HOW THE COURT INTERPRETS SECTION 6501(e)(1)(A), THE TAXPAYER WOULD PREVAIL UNDER SECTION 6229(c)(2)

B&L fully agrees with respondents that under Section 6501(e)(1)(A) an alleged overstatement of basis is not an omission from the taxpayer's gross income. *See* Resp. Br. 22-36. Respondents also are correct that the regulations do not open settled tax years and in all events fly in the face of *Colony*'s holding that Congress did not intend an omission from gross income to encompass an overstatement of basis. *Id.* at 36-50. A ruling by this Court in the taxpayer's favor on either ground advanced by respondents would conclusively resolve the dispute in B&L's favor with respect to Section 6229(c)(2).

But even if the Court were to hold that the government may overrule this Court's decision in *Colony* and apply that result retroactively to closed tax years, the government would still be unjustified in extending its view under Section 6229(c)(2). The statutory text, structure, and history of Section 6229(c)(2) establish that an alleged overstatement of basis is not an omission from a *partnership's* gross income.

The IRS regulations at issue in this case erroneously equate Sections 6501(e)(1)(A) and 6229(c)(2) and assert that, under both statutes, an overstatement of basis is an omission from gross income. Treas. Reg. §§ 301.6229(c)(2)-1(a), 301.6501(e)-1(a) (2010); *see also* Temp. Treas. Reg. §§ 301.6229(c)(2)-1T(a), 301.6501(e)-1T(a) (2009). This Court thus should make clear that regardless of Section 6501(e)(1)(A),

the taxpayer would prevail under Section 6229(c)(2). At a minimum, if the government were to prevail in this case, the Court should recognize that Section 6501(e)(1)(A) does not control the meaning of Section 6229(c)(2).

A. Sections 6501(e)(1)(A) and 6229(c)(2) Extend the Limitations Period for Tax Assessments in Different Circumstances

1. The provision at issue in this case, Section 6501(e)(1)(A), is part of a chapter in the Tax Code titled "Limitations." 26 U.S.C. ch. 66. Section 6501(a) establishes a general rule that "the amount of any tax imposed by this title shall be assessed within 3 years after the return was filed." Section 6501(e)(1)(A) provides an extended six-year limitations period "[i]f the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return."

For example, if a taxpayer with $100 of gross income omits a specific receipt or item like a dividend on the taxpayer's return, Section 6501(e)(1)(A) gives the IRS six years to assess tax on the dividend only if the dividend exceeds $25, *i.e.*, 25% of the taxpayer's reported gross income. If the dividend is less than $25, Section 6501(e)(1)(A) does not apply, and Section 6501(a) gives the IRS only three years to assess any tax.

Partnerships do not pay federal income tax, but they are required to file informational returns each year reporting "partnership items"—*i.e.*, income, gains, deductions, and credits that are passed through to partners. *See* 26 U.S.C. §§ 701, 6031,

6231(a)(3). The partners also report their respective shares of partnership items on their returns. *See* 26 U.S.C. §§ 701-704. The IRS assesses any unpaid taxes against partners, and not against the partnership.

In a subchapter titled "Tax Treatment of Partnership Items," 26 U.S.C. ch. 63, subch. C, Section 6229 sets forth a limitations period for the IRS to assess any tax attributable to a partnership item. Section 6229(a) establishes a general rule that the IRS must assess such a tax within three years after the date the partnership's return was filed or the last day for filing such return, whichever is later. Section 6229(c)(2) extends that limitations period to six years if the partnership "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in its return."

For example, if a partnership with $100 of gross income omits a partnership item on the partnership's return, Section 6229(c)(2) gives the IRS six years to assess tax attributable to that item only if the item exceeds $25. If the omitted item is less than $25, Section 6229(c)(2) does not apply, and Section 6229(a) gives the IRS only three years to assess any tax attributable to the item.

The IRS may file a timely assessment or notice attributable to a partnership item by satisfying either the general statute of limitations under Section 6501 or the alternative partnership-specific statute of limitations under Section 6229. *See Rhone-Poulenc Surfactants & Specialties L.P. v. Comm'r*, 114 T.C. 533, 541 (2000) (en banc) ("Section 6229 and Section 6501 contain alternative periods of limitation.");

Curr-Spec Partners, L.P. v. Comm'r, 579 F.3d 391, 396-97 (5th Cir. 2009) (collecting cases).

Although both Sections 6501 and 6229 provide three- and six-year statutes of limitations, the applicable limitations period varies under each statute depending on two factors. First, the limitations period under Section 6501 commences on the date the *taxpayer's* return is filed, whereas the period under Section 6229 commences on the date the *partnership's* return is filed. Second, the extended six-year period under Section 6501 applies only if an omission exceeds 25% of the *taxpayer's* gross income, whereas the six-year period under Section 6229 applies where an omission exceeds 25% of the *partnership's* gross income.

Home Concrete and B&L's case illustrate the distinction between the two statutes of limitations. In *Home Concrete*, the alleged omission exceeds 25% of the taxpayers' gross income. The government thus has relied solely on Section 6501(e)(1)(A) and has disclaimed reliance on Section 6229. *See* Resp. Br. 19 n.6. By contrast, in B&L's case, the IRS asserts that an alleged omission on a partnership's return exceeds 25% of the partnership's gross income. The alleged omission, however, is less than 25% of the gross income of the partners, which include several B&L subsidiaries. The IRS thus relies exclusively on Section 6229(c)(2) to justify the issuance of an otherwise untimely notice outside of the three-year limitations period, and Section 6501(e)(1)(A) indisputably does not apply. *Wilmington Partners L.P. v. Comm'r*, No. 10-4183 (2d Cir. argued Aug. 26, 2011).

2. Beyond their differences in operation, Congress enacted Sections 6501 and 6229 nearly three decades apart and with different language. Congress enacted Section 6501(e)(1)(A) in 1954 as the successor to Section 275(c) of the 1939 Code. *See Colony, Inc. v. Comm'r*, 357 U.S. 28, 37 (1958). Section 275(c) likewise provided an extended limitations period to assess tax where a taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return." 26 U.S.C. § 275(c) (1940). In *Colony*, this Court held that under Section 275(c) an overstatement of basis is not an "omission" from the taxpayer's gross income. 357 U.S. at 36.

Section 6501(e)(1)(A) carries forward the language of Section 275(c) with the addition of two sub-paragraphs on which the government now places almost dispositive weight. *See* U.S. Br. 20-24, 49-50. Subparagraph (i) specifies that, in the case of a trade or business, "gross income" does not include an offset for the cost of goods or services. Subparagraph (ii) provides that any items adequately disclosed on a return do not count in calculating "the amount omitted from gross income."

Congress enacted Section 6229(c)(2) in 1982 as part of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), Pub. L. No. 97-248, § 402(a), 96 Stat. 324, 659. At all times relevant to B&L's case, Section 6229(c)(2) was identical in all material respects to Section 275(c). *Compare* 26 U.S.C. § 275(c) (1940) (extending the limitations period "[i]f the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return"), *with* 26 U.S.C. § 6229(c)(2) (2000) (extending the

limitations period "[i]f any partnership omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in its return"). Section 6229(c)(2) did not contain either of the subparagraphs from Section 6501(e)(1)(A).[3]

In 2009 and 2010, the IRS issued temporary and final regulations providing that, outside the trade or business context, an overstatement of basis on a return is an omission from gross income. Treas. Reg. § 301.6501(e)-1(a) (2010); Temp. Treas. Reg. § 301.6501(e)-1T(a) (2009). The regulations thus have the effect of overruling *Colony*'s holding that an overstatement of basis is not an omission from gross income. To justify this result, the IRS relied heavily on Congress's addition in 1954 of Section 6501(e)(1)(A)(i), which, as described above, provides a special definition of "gross income" for sales of goods or services in the trade or business context. T.D. 9466, 2009-43 I.R.B. 551, *reprinted in* 74 Fed. Reg. 49,321 (Sept. 28, 2009); T.D. 9511, 2011-1 C.B. 455, *reprinted in* 75 Fed. Reg. 78,897 (Dec. 17, 2010).

---

[3] Unless otherwise indicated, all references in this brief to Section 6229(c)(2) relate to the version of that provision before Congress in 2010 amended the statute. In 2010, Congress amended Section 6229(c)(2) to cross-reference the subparagraphs under former Section 6501(e)(1)(A) (which were renumbered as Sections 6501(e)(1)(B)(i) and (ii)). *See* Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, § 513(a)(2)(B), 124 Stat. 71, 112 (2010). Nothing in the history of the 2010 amendment suggests that Congress was overruling *Colony* as applied to alleged omissions from a partnership's gross income. In all events, by its own terms, the amended provision does not apply to the tax years at issue in B&L's case. *Id.*

Although Section 6229(c)(2) contains no such subparagraph, the IRS nonetheless concluded that Sections 6501(e)(1)(A) and 6229(c)(2) have "identical meaning." 74 Fed. Reg. at 49,321. According to the preamble to the regulations, subparagraph (i) of Section 6501(e)(1)(A) "defines an omission from gross income both for purposes of section 6501 and . . . section 6229." *Id.* The IRS thus essentially cut-and-pasted subparagraph (i) from Section 6501(e)(1)(A) into the regulation interpreting Section 6229(c)(2), as if that subparagraph were part of Section 6229(c)(2), even though it is not. The regulations provide that, outside the trade or business context, an overstatement of basis is an omission from a partnership's gross income. Treas. Reg. § 301.6229(c)(2)-1(a) (2010); Temp. Treas. Reg. § 301.6229(c)(2)-1T(a) (2009).

B. *Colony* Controls the Meaning of Section 6229(c)(2)

1. As discussed, Section 6229(c)(2) is identical in all relevant respects to the limitations provision this Court interpreted in *Colony*. *See supra* pp. 11-12. Congress is presumed to be aware of this Court's precedents. *See, e.g.*, *Corley v. United States*, 129 S. Ct. 1558, 1567 (2009); *Conroy v. Aniskoff*, 507 U.S. 511, 516 (1993); *Cannon v. Univ. of Chicago*, 441 U.S. 677, 696-97 (1979). Because Congress enacted Section 6229(c)(2) against the backdrop of *Colony*, the statute must be given the same meaning that *Colony* ascribed to former Section 275(c) in 1958.

When Congress reenacts statutory language that has been given a settled interpretation by the courts, Congress is presumed to adopt that interpretation. *Lorillard v. Pons*, 434 U.S. 575, 580 (1978). This Court has "often observed that when 'judicial interpretations have settled the meaning of an

existing statutory provision, repetition of the same language in a new statute indicates, as a general matter, the intent to incorporate its . . . judicial interpretations as well.'" *Jerman v. Carlisle, McNellie, Rini, Kramer & Ulrich LPA*, 130 S. Ct. 1605, 1616 (2010) (alteration in original) (quoting *Bragdon v. Abbott*, 524 U.S. 624, 645 (1998)).

Congress enacted Section 6229(c)(2) in 1982 more than two decades after *Colony* resolved the meaning of identical language in Section 275(c). Congress's reenactment of the same statutory language in 1982 after this Court conclusively resolved its meaning shows that Section 6229(c)(2) incorporates the meaning settled by *Colony*. At that time, no one—not even the IRS—had yet suggested that the Court's interpretation in *Colony* of when an overstatement of basis constitutes an omission from gross income was rendered obsolete by Congress's addition of the subparagraphs in Section 6501(e)(1)(A). Indeed, in 1976, the IRS recognized *Colony* as the "landmark" case on the meaning of Section 6501(e). I.R.S. Gen. Counsel Mem. 36,856 (Sept. 21, 1976). It is thus implausible that Congress in enacting Section 6229(c)(2) intended to depart from this Court's interpretation of the same text a quarter-century earlier in *Colony*.

Moreover, from 1982 to 2010, the critical statutory language remained untouched through substantive amendments to Section 6229 and Congress's reenactment of the Internal Revenue Code in 1986. *See* Pub. L. No. 99-514, § 1875(d)(1), 100 Stat. 2085, 2896 (1986); Pub. L. No. 100-647, § 1018(o)(3), 102 Stat. 3342, 3585 (1988); Pub. L. No. 105-34, §§ 1233, 1235(a), 111 Stat. 788, 1023-25 (1997). Thus, as in

Colony, under Section 6229(c)(2), an overstatement of basis is not an omission from gross income.

In light of Section 6229(c)(2)'s unambiguous meaning, the IRS's 2009 and 2010 regulations purporting to assign the opposite meaning are invalid and entitled to no deference. By reenacting the precise language that *Colony* authoritatively construed and thereby adopting *Colony*'s holding, Congress in 1982 "directly addressed the precise question at issue." *Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 843 (1984). In other words, even if the meaning of Section 275(c) were somehow ambiguous when the Court first construed the language in *Colony*—and it manifestly was not, *see* Resp. Br. 36-39—the meaning of the statutory text had long been resolved by 1982 when Congress enacted Section 6229(c)(2).

2. The government's two arguments for casting aside *Colony* with respect to Section 6501(e)(1)(A) are wrong. *See* Resp. Br. 33-35. In any event, those arguments are inapplicable to Section 6229(c)(2) and only reinforce that *Colony* controls the meaning of Section 6229(c)(2).

First, the government argues that Section 6501(e)(1)(A) is not controlled by *Colony* because of two "adjacent provisions"—Sections 6501(e)(1)(A)(i) and 6501(e)(2)—that "were not part of the statutory scheme before the Court in *Colony*." U.S. Br. 20, 49. Although the government's reasoning is wrong, *see* Resp. Br. 29-36, the government's all but dispositive reliance on these adjacent provisions fatally undermines its position under Section 6229(c)(2).

Section 6501(e)(1)(A)(i) provides that in the context of sales of "goods or services" by a "trade or business," the term "gross income" means the taxpayer's total receipts *before* deducting its costs. The government argues that, in all other contexts, gross income must mean receipts *after* deducting basis, and thus an overstatement of basis would lead to an omission from gross income. *See* U.S. Br. 20-23. As respondents explain, however, subparagraph (i) supports *Colony*'s holding, and giving effect to the *Colony* rule does not strip subparagraph (i) of independent meaning or practical significance (as the government itself acknowledges, *see* U.S. Br. 22-23).

Section 6501(e)(2), which applies to gift and estate taxes, provides an extended six-year limitations period if the taxpayer omits "items includable in such gross estate or such total gifts." The government attributes meaning to Congress's use of the word "items" in Section 6501(e)(2) versus the word "amount" in Section 6501(e)(1)(A). According to the government, an overstatement of basis understates the "amount" of gross income, even though it does not omit any "item." U.S. Br. 23-24. Again, the government's reliance on that provision is dubious. *See* Resp. Br. 35 n.14.

But the government's arguments fatally undermine its position in B&L's case because Congress enacted Section 6229(c)(2) *without* these provisions, and the legislature instead employed language identical in all relevant respects to the statute before the Court in *Colony*. If it is so significant that these provisions did not appear in the statute the Court confronted in *Colony*, then it is equally significant that they do not appear in Section 6229. In other words, the more that the government relies on Sections

6501(e)(1)(A)(i) and 6501(e)(2) to support its interpretation of Section 6501(e)(1)(A), the more the government erodes any basis for its interpretation of Section 6229(c)(2).

The government cannot have its cake and eat it too. If *Colony* does not govern Section 6501(e)(1)(A) because Congress added these adjacent provisions, then Congress's omission of those provisions from Section 6229(c)(2) confirms that Congress intended *Colony* to control the meaning of an omission from a partnership's gross income.

Second, the government argues that *Colony* does not control the meaning of Section 6501(e)(1)(A) because the IRS was free to reinterpret the meaning of the statute by regulation. Because *Colony* observed that the language of Section 275(c) was ambiguous, the government argues that the IRS in 2009 could properly re-interpret the same language in Section 6501(e)(1)(A), which was enacted four years *before Colony*. *See* U.S. Br. 13-14. That too is incorrect. *See* Resp. Br. 36-39.

Regardless, Congress enacted Section 6229(c)(2) two decades *after Colony*. Insofar as Section 6229(c)(2) is concerned, *Colony* was clearly decided at *Chevron* step one, definitively resolving the interpretive question and removing any regulatory discretion from the IRS. Congress's enactment of Section 6229(c)(2) after *Colony* thus bars the government from relying on *National Cable & Telecommunications Ass'n v. Brand X Internet Services*, 545 U.S. 967 (2005), as the government attempts to do with Section 6501(e)(1)(A). Even if the government could stretch *Brand X* in that respect for Section

6501(e)(1)(A), *Brand X* would not help the government with respect to Section 6229(c)(2).[4]

3. In any event, the regulations' stated justifications for equating Sections 6501(e)(1)(A) and 6229(c)(2) are meritless. In the preamble to its temporary regulations, the IRS asserted that Congress presumptively intended "to give the language in section 6229, which is identical to language in section 6501, identical meaning." 74 Fed. Reg. at 49,321. As described above, however, Section 6229(c)(2) is not identical to Section 6501(e)(1)(A)—Section 6229(c)(2) at all relevant times did not contain the "adjacent provisions" (U.S. Br. 20) from Section 6501(e) on which the government now places near-dispositive weight.

The absence of such provisions thus triggers the opposite presumption that statutes with different text have different meanings. "Congress acts intentionally and purposely in the disparate inclusion or exclusion" of statutory language. *Russello v. United States*, 464 U.S. 16, 23 (1983). "[N]egative implications raised by disparate provisions are strongest when the portions of a statute treated differently had already been joined together and were being considered

---

[4] No court of appeals has directly addressed these distinctions between Sections 6501(e)(1)(A) and 6229(c)(2). In *Intermountain*, the taxpayer at oral argument asserted, for the first time, that "this case is not about [section] 6501 but only section 6229 given the Tax Court's observation that where, as here, the Commissioner has adjusted only partnership items, only section 6229(c)(2) applies." 650 F.3d at 699 (internal quotation marks omitted). The D.C. Circuit, however, refused to consider this argument and "treat[ed] as forfeited any argument that the two sections might have different meanings outside the trade or business context, focusing our analysis, as have the parties themselves, on the earlier enacted section 6501(e)(1)(A)." *Id.*

simultaneously when the language raising the implication was inserted." *Lindh v. Murphy*, 521 U.S. 320, 330 (1997).

Again, if the government were right that Congress's enactment of Sections 6501(e)(1)(A)(i) and 6501(e)(2) changed the meaning of the language previously codified as Section 275(c), then Congress's enactment of the identical language in Section 6229(c)(2) without those adjacent provisions removes any basis for distinguishing *Colony*. The IRS itself previously recognized that Congress "was aware of" Section 6501(e)(1)(A)'s subparagraphs when it enacted Section 6229(c)(2), yet Congress "consciously left out" those subparagraphs. I.R.S. F.S.A. 1591, 1995 FSA LEXIS 354 (May 10, 1995).

The regulations also assert that because Section 6501(e)(1)(A)(i) defines "gross income" in the trade or business context, there is no need for Congress to "redefine the same phrase" in Section 6229(c)(2). 74 Fed. Reg. at 49,321. The statutory text flatly contradicts this argument. The definition of "gross income" in Section 6501(e)(1)(A)(i) expressly applies only "[f]or purposes of *this subparagraph*," and therefore does not apply to the separate statutory provision of Section 6229(c)(2). (Emphasis added).

The regulations further cite Section 6501(n)(2), which merely states that "[f]or extension of period in the case of partnership items . . . see section 6229." 26 U.S.C. § 6501(n)(2). Nothing in that language remotely suggests that Congress incorporated subparagraphs (i) and (ii) from Section 6501(e)(1)(A) into Section 6229(c)(2). In all events, the limitations period under Section 6501(e)(1)(A) has no relevance in cases such as B&L's where the alleged omission is less than 25% of the taxpayer's gross income. In

such cases, Section 6229 does not "extend" Section 6501(e)(1)(A), because the IRS cannot meet the 25% threshold for application of Section 6501(e)(1)(A).

The IRS, moreover, has argued that it would be incongruent to treat a transaction differently for limitations purposes "based on the happenstance of whether the transaction is reported on a partnership return rather than a partner's return." 74 Fed. Reg. at 49,321. But the IRS itself is the source of any unwarranted disparate treatment, based on its strained claim that, contrary to the holding of *Colony*, an overstatement of basis on a taxpayer's return can trigger the extended limitations period under Section 6501(e)(1)(A). If the IRS believes it is important for Sections 6501(e)(1)(A) and 6229(c)(2) to be read in harmony, the proper course is to follow *Colony* with respect to both statutes, and not to compound one error of statutory interpretation with another.

It only makes sense to say that Sections 6229(c)(2) and 6501(e)(1)(A) have the "identical meaning" if that meaning is the one that this Court recognized in *Colony*. But if, as the government contends, the addition of subparagraph (i) *changed* the meaning of the general rule set forth in Section 6501(e)(1)(A), then Congress's *omission* of subparagraph (i) in Section 6229(c)(2) must be viewed as an act of great significance when it comes to the meaning of Section 6229(c)(2). The government cannot have it both ways.

II. THE GOVERNMENT'S POSITION WOULD APPLY TO LEGITIMATE BUSINESS TRANSACTIONS; AND IT IS UNNECESSARY TO COMBAT ABUSIVE TAX SHELTERS

The government asserts that a six-year limitations period is necessary to ferret out "Son-of-BOSS tax shelters" and other illegitimate "tax-avoidance schemes." U.S. Br. 6 n.2, 25. The government's brief mentions "Son-of-BOSS" transactions no less than a dozen times. U.S. Br. 3, 4, 5, 6, 8, 25. The IRS likewise has based its interpretation of Section 6229(c)(2) on the purported need to combat Son-of-BOSS transactions and other abusive tax shelters. 74 Fed. Reg. at 49,321. But the government's interpretation of Sections 6501 and 6229 would apply to legitimate transactions and abusive tax evasion schemes alike.

In any event, the government does not need to stretch the language of the Internal Revenue Code and overrule the half-century-old precedent of *Colony* to combat transactions the IRS deems to be abusive. Congress in 2004 added to the Code an open-ended limitations period to address such schemes. *See* American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 814(a), 118 Stat. 1418, 1581 (codified at 26 U.S.C. § 6501(c)(10)). The Court should not excuse the government from its own negligence or oversight in waiting more than three years to question an item on a tax return.

A. Limitations periods "are by definition arbitrary, and their operation does not discriminate between the just and the unjust claim." *Chase Sec. Corp. v. Donaldson*, 325 U.S. 304, 314 (1945); *accord Plaut v. Spendthrift Farm, Inc.*, 514 U.S. 211, 264 n.20 (1995)

(Stevens, J., dissenting) (quoting same); *In re Becker*, 407 F.3d 89, 104 (2d Cir. 2005) (same). The government thus cannot justify its strained interpretation of the IRS limitations periods simply because having more time would help the IRS fight abusive tax shelters.

The general statutes of limitations under Sections 6501 and 6229 on their face are not restricted to illegitimate tax-avoidance schemes. Those limitations periods govern tax assessments arising from legitimate business transactions and abusive tax shelters alike. For example, B&L's case does not involve a Son-of-BOSS scheme or any other listed transaction, and the IRS has never contended otherwise. *See Intermountain*, 650 F.3d at 699 (recognizing that B&L's case involves "no Son of Boss tax shelter allegation"); U.S. Cert. Reply at 4 (similar).

Rather, B&L's dispute with the IRS concerns the proper characterization of a series of legitimate business transactions for purposes of determining a partnership's basis in a $550 million Note (and a partner's corresponding basis in its partnership interest). Nevertheless, the IRS relies on an extended limitations period to justify its untimely assessment of hundreds of millions of dollars in taxes, penalties, and interest based on those transactions.

In 1993, B&L and unrelated parties created a partnership, Wilmington Partners L.P. ("Wilmington"), as part of a business transaction to raise capital. B&L's partnership contribution included several operating businesses and a $550 million Note, made by one B&L affiliate and payable to another. On its 1993 partnership return, Wilmington took a basis of $550 million in the Note—its face amount and

undisputed fair market value. After conducting an extensive audit of Wilmington's 1993 return, the IRS notified Wilmington in 2000 that it would make "no adjustments." Brief for the Appellant at 8, *Wilmington Partners*, No. 10-4183 (2d Cir.).

In 1999, the partners restructured Wilmington and again took a basis of $550 million in the Note on its partnership returns that year. In 2004, more than three years after Wilmington filed its 1999 returns, the IRS commenced an audit. In 2006, the IRS purported to reduce Wilmington's basis in the 1993 Note from $550 million to zero. Based on this change, the IRS has suggested that B&L owes hundreds of millions of dollars in taxes, penalties, and interest. B&L's case thus illustrates that the IRS is attempting to apply a six-year limitations period outside the context of abusive tax shelters. Indeed, citing B&L's case, the government at the certiorari stage advised this Court that the issues in this case can "arise in cases that do not involve Son-of-BOSS shelters." U.S. Cert. Reply at 4.

B. Going forward, disputes over legitimate transactions likely are the *only* types of cases that will be governed by the general statutes of limitations for tax assessments. Congress in 2004 amended Section 6501 to provide a forgiving limitations period for any assessment arising from a "listed transaction." American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 814, 118 Stat. 1418 (codified at 26 U.S.C. § 6501(c)(10)). A listed transaction is a "transaction which is the same as, or substantially similar to, a transaction specifically identified by the [IRS] as a tax avoidance transaction." 26 U.S.C. § 6707A(c)(2).

The Code requires any taxpayer who engages in a listed transaction to make detailed disclosures to the IRS regarding the transaction. 26 U.S.C. § 6011. Under the 2004 amendment to Section 6501, "[i]f a taxpayer fails to include on any return or statement for any taxable year any information with respect to a listed transaction . . . which is required . . . to be included with such return or statement, the time for assessment of any tax . . . with respect to such transaction shall not expire" until one year after the taxpayer makes the required disclosure. 26 U.S.C. § 6501(c)(10); *see also* Elliot Pisem & Jason K. Binder, Blak *Affirms the Necessity of Raising S/L Defenses Early in TEFRA Partnership Proceedings*, 112 J. Tax'n 222, 222 (2010) (noting that Section 6501(c)(10) can "operate to extend the period of limitations . . . indefinitely"); Joshua D. Blank, *What's Wrong with Shaming Corporate Tax Abuse*, 62 Tax L. Rev. 539, 573-74 (2009) ("[I]n cases where a [taxpayer] does not disclose its participation in a listed transaction, the statute of limitations may never expire.").

The tolling feature of Section 6501(c)(10) permits the IRS to assess any additional tax for abusive tax shelters without resort to the extended limitations periods at issue in this case and B&L's case. And where applicable, the IRS may invoke exceptions to the general limitations periods that allow the IRS "at any time" to assess any tax stemming from a "false or fraudulent" return or "willful" evasion. 26 U.S.C. §§ 6229(c)(1), 6501(c)(1), (2).

By contrast, in cases that do not involve any fraud or willful evasion, and where the taxpayer has disclosed the disputed item in its return, the IRS is not entitled to an open-ended limitations period to assess taxes. The government asserts that "a basis overstatement will typically be as difficult to detect as an understatement of sale price." U.S. Br. 11. But the same is true of an overstated deduction, which indisputably does not trigger an extended limitations period under Section 6501 or 6229. *See* Resp. Br. 24-25.

The government's position thus would create the very "patent incongruity" that this Court specifically avoided in *Colony*—whereby an overstatement of basis would give the IRS extra time, but an "overstated deduction" on the same return would not. *Colony*, 357 U.S. at 36. Congress could not plausibly have intended such an inconsistent approach to the limitations periods for IRS tax assessments.

C. This Court should apply to the IRS the same principle that the IRS seeks to apply to taxpayers: speak now or forever hold your peace. "From the beginning of [the nation's] history, the United States has insisted upon a prompt claim for refund as a condition of refunding taxes that have been improperly collected." Brief for United States at 16, *United States v. Brockamp*, 519 U.S. 347 (1997) (No. 95-1225). Adopting the government's position here would create a one-way-ratchet wherein taxpayers are held to rigid compliance with limitations periods, but the IRS is not.

The government's approach would excuse the IRS from its own lethargy and failures and would deprive taxpayers of certainty and finality concerning their tax obligations arising from legitimate business transactions. As the United States has advised this Court, "[t]here is manifestly an imperative need for predictability and certainty in the processes" for resolving tax disputes. *Id.* at 25. Yet here the government makes a mockery out of that principle by promulgating regulations to upset decades of settled expectations surrounding the rule of *Colony*.

B&L's case is a particularly egregious example of the government's overreaching. There, the IRS had two separate opportunities to investigate the basis of the Note in reviewing Wilmington's 1993 and 1999 partnership returns. In 1993, the IRS conducted a timely audit and concluded that "no adjustments" were necessary. For the 1999 return, the IRS waited more than three years before even commencing an audit.

Moreover, Wilmington filed two 1999 partnership returns, and while the IRS timely obtained an extension of the limitations period for one return, it inexplicably failed to request an extension for the other, forcing the IRS to rely on an extended statute of limitations. Had the shoe been on the other foot, the IRS surely would have argued that the taxpayer was out of luck. Finality should be a two-way street.

Yet, after losing its argument in the Tax Court, the IRS took the extraordinary step of trying to extend retroactively the statute of limitations and overrule *Colony* by regulation, for purposes of both Sections 6501 and 6229. This Court should reject the government's overreaching as to respondents, B&L, and taxpayers generally.

CONCLUSION

For the reasons explained by respondents, the Court should affirm the decision below. If the Court disagrees, however, it should make clear that its decision does not endorse the government's reading of the limitations period under Section 6229(c)(2).

Respectfully submitted,

LISA S. BLATT
Counsel of Record
ANTHONY J. FRANZE
R. STANTON JONES
ARNOLD & PORTER LLP
555 12th Street, N.W.
Washington, DC 20004
(202) 942-5000
lisa.blatt@aporter.com

Counsel for Amicus Curiae
Bausch & Lomb Incorporated

December 22, 2011

AMICUS CURIAE BRIEF

RECORD
AND
BRIEFS

No. 11-139

In the
Supreme Court of the United States

UNITED STATES OF AMERICA,
Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF OF DANIEL S. BURKS AND REYNOLDS PROPERTIES, L.P. AS *AMICI CURIAE* IN SUPPORT OF RESPONDENTS

JOEL N. CROUCH
Counsel of Record
DAVID E. COLMENERO
MEADOWS, COLLIER, REED,
COUSINS, CROUCH &
UNGERMAN, L.L.P.
901 MAIN STREET, SUITE 3700
DALLAS, TX 75202
(214) 744-3700 TELEPHONE
(214) 747-3732 FACSIMILE
jcrouch@meadowscollier.com

Counsel for Amicus Curiae
Daniel S. Burks

ANTHONY P. DADDINO
MEADOWS, COLLIER, REED,
COUSINS, CROUCH &
UNGERMAN, L.L.P.
901 MAIN STREET, SUITE 3700
DALLAS, TX 75202
(214) 744-3700 TELEPHONE
(214) 747-3732 FACSIMILE
adaddino@meadowscollier.com

Counsel for Amicus Curiae
Reynolds Properties, L.P.

December 22, 2011

Becker Gallagher · Cincinnati, OH · Washington, D.C. · 800.890.5001

Library of Congress
Law Library

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

INTEREST OF THE AMICI CURIAE 1

INTRODUCTION AND STATEMENT OF ISSUE 1

SUMMARY OF ARGUMENT 2

ARGUMENT 3

1. THE REGULATION DOES NOT APPLY BECAUSE THE IRS DID NOT TIMELY MAIL THE FPAA. . . 3

2. THE LACK OF A FINAL DECISION IN THE LITIGATION DOES NOT MAKE THE REGULATION APPLICABLE. 7

3. THE REGULATION IS NOT RETROACTIVE AND CANNOT BE APPLIED RETROACTIVELY. 11

4. APPLYING THE REGULATION CREATES A "HEADS THE GOVERNMENT WINS – TAILS THE TAXPAYER LOSES" SITUATION THAT FRUSTRATES THE PURPOSE BEHIND STATUTES OF LIMITATION. 14

CONCLUSION 16

TABLE OF AUTHORITIES

CASES

Agway, Inc. v. United States,
524 F.2d 1194 (Ct. Cl. 1975) 11

Bowles v. Seminole Rock & Sand Co.,
325 U.S. 410 (1945) 8

Burks v. United States,
633 F.3d 347 (5th Cir. 2011), *petition for cert. filed*, No. 11-178 (U.S. Aug. 11, 2011) 9

Carpenter Family Invs., LLC, v. Comm'r,
136 T.C. 373 (2011) 9

Chenault v. U.S. Postal Service,
37 F.3d 535 (9th Cir. 1994) 12, 13, 14

Chimblo v. Comm'r,
177 F.3d 119 (2d Cir. 1999) 14

Clodfelter v. Comm'r,
527 F.2d 754 (9th Cir. 1975) 5

Colony, Inc. v. Comm'r,
357 U.S. 28 (1958) 1, 2

Comm'r v. S. Frieder & Sons Co.,
247 F.2d 834 (3d Cir. 1957) 4, 8

Crowell v. Comm'r,
102 T.C. 683 (1994) 14

Frieling v. Comm'r,
81 T.C. 42 (1983) 5

Grapevine Imports, Ltd. v. United States,
636 F.3d 1368 (Fed. Cir. Mar. 11, 2011), *petition for cert. filed*, No. 11-163 (U.S. Aug. 5, 2011) . 10

Greve v. Comm'r,
42 B.T.A. 142 (1940) 6, 8

Hughes Aircraft Co. v. United States,
520 U.S. 939 (1997) 13, 14

Intermountain Ins. Svc. of Vail v. Comm'r,
134 T.C. 211 (2010), *rev'd*, 650 F.3d 691 (D.C. Cir. 2011), *petition for cert. filed*, No. 11-663 (U.S. Nov. 16, 2011) 9, 10

Kaplan v. United States,
133 F.3d 469 (7th Cir. 1998) 14

Landgraf v. USI Film Prods.,
511 U.S. 244 (1994) 13

Pac. Nat'l Bank v. Comm'r,
91 F.2d 103 (9th Cir. 1937) 11, 12

Reddock v. Comm'r,
72 T.C. 21 (1979) 4, 5, 6, 8

Rothensies v. Elec. Storage Battery Co.,
329 U.S. 296 (1946) 16

Salman Ranch, Ltd. v. Comm'r,
647 F.3d 929 (10th Cir. May 31, 2011), *petition for cert. filed*, No. 11-582 (U.S. Nov. 7, 2011) . 10

Sealy Power, Ltd v. Comm'r,
46 F.3d 382 (5th Cir. 1995) 5

St. Joseph Lease Capital Corp. v. Comm'r,
235 F.3d 886 (4th Cir. 2000) 4

Weiner v. United States,
389 F.3d 152 (5th Cir. 2004) 14

STATUTES

I.R.C. § 6229(d) 4

I.R.C. § 6501 ..... 4, 9

I.R.C. § 6501(e) 2

I.R.C. § 6503 ..... 4, 9

I.R.C. § 6503(a) 3, 6

I.R.C. § 6503(a)(1) 3

I.R.C. § 7805 11

I.R.C. § 7805(b) 11

REGULATIONS

Treas. Reg. § 301.6501(e)-1 1

Treas. Reg. § 301.6501(e)-1(e)(1) 3

RULES

SUP. CT. R. 37.3(a) 1

SUP. CT. R. 37.6 1

OTHER

BLACK'S LAW DICTIONARY 592 (9th ed. 2009) 9

T.D. 9511, 75 Fed. Reg. 78897-01 (2010) . . 7, 10, 11

INTEREST OF THE AMICI CURIAE

Amici curiae Daniel S. Burks and Reynolds Properties, L.P. are parties to pending litigation involving the same issue present in this case, and therefore, they are interested in the outcome of this litigation.[1] *See United States v. Burks, petition for cert. filed*, No. 11-178 (U.S. Aug. 11, 2011); *Reynolds Properties, L.P. v. Comm'r*, Nos. 10-72406 and 10-73376 (9th Cir.).

INTRODUCTION AND STATEMENT OF ISSUE

Much ink has been spilled in the federal courts across the United States regarding this Court's decision in *Colony, Inc. v. Commissioner*, 357 U.S. 28 (1958), and the level of deference to be afforded Treasury Regulation § 301.6501(e)-1 (the "Regulation"), which flagrantly seeks to trump *Colony* and congressional intent. This brief does not add to such body of work, but rather addresses a much simpler issue present in *United States v. Home Concrete & Supply, LLC* and the many other cases standing behind it. That is, assuming this Court

---

[1] This amicus brief is filed with the consent of the parties. *See* SUP. CT. R. 37.3(a). Petitioner filed a letter consenting to the filing of amicus briefs on November 23, 2011. Respondent filed a letter consenting to the filing of amicus briefs on November 22, 2011. Further, pursuant to Rule 37.6, the amici curiae submitting this brief and their counsel hereby represent that neither party to this case nor their counsel authored any part of this brief, and that no person other than amici curiae made a monetary contribution toward the preparation or submission of this brief.

reaches the issue of the Regulation,[2] does the Regulation apply to a tax year if the limitations period for that year was closed on September 24, 2009? The effective-date provision of the Regulation definitively answers this question: "No."

SUMMARY OF ARGUMENT

The Regulation is clear. It applies only to tax years for which the limitations period was open on or after September 24, 2009. The limitations period for the tax year at issue was closed on that date because the IRS did not timely mail the Notice of Final Partnership Administrative Adjustment ("FPAA"). On the FPAA mailing date, the 3-year limitations period had expired, the Regulation did not exist, and under this Court's precedent in *Colony*, the 6-year limitations period did not apply. Because the FPAA was not timely, it could not and did not suspend the limitations period, and thus, the limitations period was not further suspended by the district court litigation. The Government's argument for applying the Regulation based on a lack of final decision in this case is wholly without merit.

While the Government urges that, if necessary, this Court may apply the Regulation retroactively, there is no legal basis for doing so. The Government issued the Regulation with a contemporaneous effective date, and has publicly declared that the Regulation is not

---

[2] This brief assumes the Court holds that *Colony* applies to the 1954 version of the Internal Revenue Code, under which a basis overstatement does not give rise to an "omission" from gross income triggering the 6-year limitations period under I.R.C. § 6501(e).

retroactive. Also, applying the Regulation retroactively has the legally-impermissible effect of reopening a closed tax year and stripping the taxpayer of its substantive rights against an untimely tax assessment. It places taxpayers in a "Heads the Government Wins, Tails the Taxpayer Loses" situation, wherein the taxpayers either voluntarily, or by virtue of challenging the IRS, forfeit their statute-of-limitations defenses. For these reasons, the Regulation cannot and should not apply.

ARGUMENT

1. THE REGULATION DOES NOT APPLY BECAUSE THE IRS DID NOT TIMELY MAIL THE FPAA.

The IRS's untimely mailing of the FPAA cannot operate to reopen a limitations period that has already expired. The tax year at issue was closed when the IRS issued the FPAA and therefore was also closed on September 24, 2009 when the Regulation took effect. For this reason, the Regulation does not apply.

The Regulation states that it applies "to taxable years with respect to which the period for assessing tax was open on or after September 24, 2009." Treas. Reg. § 301.6501(e)-1(e)(1). The only manner in which the limitations period for the tax year at issue could be considered open on September 24, 2009 is if the district court litigation somehow reopened the period under I.R.C. § 6503(a).[3] This provision, and its

---

[3] *See* I.R.C. § 6503(a)(1) ("The running of the period of limitations provided in section 6501 or 6502 (or section 6229[)] . . . in respect of any deficiency as defined in section 6211 . . . shall (after the

partnership counterpart,[4] operate to suspend the limitations period upon the IRS's timely mailing of a notice of deficiency or FPAA – not reopen a closed period.[5] The Third Circuit highlighted this timeliness requirement and the interplay of §§ 6501 and 6503 in *Commissioner v. S. Frieder & Sons Co.*:

> [T]he combined effect of Section 275 and Section 277 [predecessors to §§ 6501 and 6503, respectively] is to cause the three year statute of limitations on excess profits tax deficiency assessments to run until it shall be suspended by the Commissioner's issuance of such a deficiency notice as is a statutory prerequisite to assessment. But if the statutory period has

---

mailing of a notice under section 6212(a)) be suspended for the period during which the Secretary is prohibited from making the assessment or from collecting by levy or a proceeding in court (and in any event, if a proceeding in respect of the deficiency is placed on the docket of the Tax Court, until the decision of the Tax Court becomes final), and for 60 days thereafter.").

[4] I.R.C. § 6229(d) ("If notice of a final partnership administrative adjustment with respect to any taxable year is mailed to the tax matters partner, the running of the period specified in subsection (a) (as modified by other provisions of this section) shall be suspended—for the period during which an action may be brought under section 6226 (and, if a petition is filed under section 6226 with respect to such administrative adjustment, until the decision of the court becomes final), and for 1 year thereafter.").

[5] *See St. Joseph Lease Capital Corp. v. Comm'r*, 235 F.3d 886, 888-90 (4th Cir. 2000) (timely mailing of the notice of deficiency is the crucial act suspending the limitations period); *Reddock v. Comm'r*, 72 T.C. 21, 27-28 (1979).

> fully run before the giving of such notice, the bar is not removed by that untimely notice.

247 F.2d 834, 837 (3d Cir. 1957).[6]

It is a well-settled rule that the timeliness of an IRS notice of deficiency or FPAA is determined on the mailing date of the notice applying the law in effect at that time. *See, e.g., Frieling v. Comm'r*, 81 T.C. 42, 54 (1983) ("We have held that the date the notice of deficiency is mailed . . . determines whether that notice is timely."); *see also Clodfelter v. Comm'r*, 527 F.2d 754, 757 (9th Cir. 1975) (timeliness of a notice of deficiency determined based on the mailing date); *Reddock v. Comm'r*, 72 T.C. 21, 27-28 (1979). On the mailing date of the FPAA in this case, the 3-year limitations period for the tax year at issue had expired and the Regulation did not exist. The FPAA was therefore untimely.

Because the IRS did not timely mail the FPAA, the FPAA could not operate to suspend the limitations period. As the Tax Court keenly noted decades ago, "[t]here can be no suspension of the running after the

---

[6] These decisions, addressing the suspension of the limitations period with respect to timely issued notices of deficiency, apply with equal force to FPAAs. *See Sealy Power, Ltd v. Comm'r*, 46 F.3d 382, 385-86 (5th Cir. 1995) ("[A]n FPAA is the functional equivalent of a notice of deficiency. Both the FPAA and the notice of deficiency serve to notify affected taxpayers that the Commissioner has made a final administrative determination of their liability for particular tax years. We therefore analyze the FPAA here the same way that we would analyze a notice of deficiency.").

period has completely run." *Greve v. Comm'r*, 42 B.T.A. 142, 142 (1940).

The Tax Court affirmed this truism years later in *Reddock v. Commissioner*, 72 T.C. 21 (1979). In that case, the IRS initially mailed a notice of deficiency to the taxpayer at the wrong address. The IRS thereafter mailed a second notice of deficiency to the correct address, but after the limitations period had expired. The Tax Court dismissed the first notice as invalid. Regarding the second notice, the Tax Court found that the limitations period had expired when the IRS mailed it; and consequently, the untimely notice did not suspend the limitations period under § 6503(a). This is true because after the limitations period expires, "[t]he Secretary no longer possessed the power to make a valid assessment or to issue a notice of deficiency which, under section 6503(a), would suspend the running of the statute of limitations." *Reddock*, 72 T.C. at 26.

Because the untimely FPAA did not suspend the limitations period, it was impossible for the limitations period to be further suspended by the district court litigation. *See Greve*, 42 B.T.A. at 144 ("the running of the period could not be suspended by anything which happened [after issuance of notice]."). The mere fact that the taxpayers exercised their right of judicial review of the FPAA's adjustments had no effect on the limitations period or their statute-of-limitations defenses. *See Reddock*, 72 T.C. at 27 ("By filing their petition in this Court, petitioners waived nothing.").

At the end of the day, the limitations period was closed when the IRS mailed the FPAA in this case. It remained closed when the taxpayers petitioned for

judicial review and throughout the district court litigation. And the limitations period was closed on September 24, 2009 when the Regulation took effect. The Regulation therefore does not apply by its own terms.

2. THE LACK OF A FINAL DECISION IN THE LITIGATION DOES NOT MAKE THE REGULATION APPLICABLE.

The Government attempts to avoid this literal result by arguing that the Regulation applies because there was not yet a final decision in the litigation. Although the Regulation states that it only applies to tax years open on September 24, 2009, the Government argues that this language somehow includes tax years "that are the subject of any case pending before any court of competent jurisdiction (including the United States Tax Court and Court of Federal Claims) in which a decision had not become final (within the meaning of section 7481)." T.D. 9511, 75 Fed. Reg. 78897-01, 78898 (2010).

The Government raises a specious and ultimately unsupportable argument. The lack of a final decision does not answer the question posed by the Regulation's effective date provision – is the limitations period for the tax year open on September 24, 2009? The weakness in the Government's position is that it assumes the litigation suspended the limitations period. Such assumption is false. The limitations period was closed when the IRS issued the FPAA and it cannot be reopened by the filing of a lawsuit.

The Government ignores the infirmity of its assumption and instead seeks deference for its "interpretation" of the effective date provision of the

Regulation. The Government seeks that to which it is not entitled. This Court declared long ago that an agency's interpretation of its promulgated rules is not entitled to deference if the interpretation is either plainly erroneous or inconsistent with the regulation. *See Bowles v. Seminole Rock & Sand Co.*, 325 U.S. 410, 414 (1945).[7] The Government's "interpretation" of the effective date of the Regulation is both.

The Government's "interpretation" is plainly erroneous because it is based on a faulty legal premise: that the litigation somehow held open the limitations period. This did not occur here because the IRS failed to timely mail the FPAA. There can be no suspension of a limitations period that has already expired. *S. Frieder & Sons*, 247 F.2d at 837; *Reddock*, 72 T.C. at 26-27; *Greve*, 42 B.T.A. at 142, 144. Thus to apply the Regulation here – where the limitations period was not open on the Regulation's effective date – is plainly erroneous.

---

[7] In *Bowles*, a crushed-stone company challenged the Government's interpretation of a regulation promulgated by the Office of Price Administration. The regulation imposed a maximum price at which building materials could be delivered. Maximum price was defined as the "highest price charged" during a specific period of time. The Government interpreted "highest price charged" as including the price at which goods were delivered during the relevant period, even though the goods were sold under an order pre-dating the relevant period. In deciding that case, this Court set the framework for evaluating agency interpretations of their own regulations, holding that the interpretation "becomes of controlling weight unless it is plainly erroneous or inconsistent with the regulation." *Bowles v. Seminole Rock & Sand Co.*, 325 U.S. 410, 414 (1945).

The Government's "interpretation" is also plainly erroneous because it requires this Court to give effect to the Regulation in applying the effective date provision of the Regulation. Such argument demeans the generally-accepted definition of "effective date." Black's Law Dictionary (9th ed.) defines effective date as "[t]he date on which a statute, contract, insurance policy, or other such instrument becomes enforceable . . ." BLACK'S LAW DICTIONARY 592 (9th ed. 2009). Applying this definition, the Regulation became enforceable on September 24, 2009. The Government would have this Court apply the unenforceable provisions of the Regulation in order to make the Regulation enforceable. This circular method of construing an effective date provision nullifies the whole point of having an effective date, and, as the Tax Court perceptively noted, is "irreparably marred by circular, result-driven logic" which has no place in the tax laws. *Intermountain Ins. Svc. of Vail v. Comm'r*, 134 T.C. 211, 219 (2010), *rev'd*, 650 F.3d 691 (D.C. Cir. 2011), *petition for cert. filed*, No. 11-663 (U.S. Nov. 16, 2011); *Carpenter Family Invs., LLC, v. Comm'r*, 136 T.C. 373, 379-80 (2011) (same ruling); *see also Burks v. United States*, 633 F.3d 347, 360 (5th Cir. 2011), *petition for cert. filed*, No. 11-178 (U.S. Aug. 11, 2011) (rejecting the Government's "circular argument that the Regulations apply to the taxpayers because the statute of limitations remains open under the language of the newly promulgated Regulations").

The Government's "interpretation" should also be rejected because it is inconsistent with the Regulation and the Treasury's issuing statements. Giving proper consideration to I.R.C. §§ 6501 and 6503, the only conceivable manner for the Regulation to apply to the tax year at issue is for this Court to place the

Regulation in effect at the time the IRS mailed the FPAA. In other words, this Court must give the Regulation retroactive effect. This would be wholly inconsistent with the Regulation's contemporaneous effective date and the Treasury's public pronouncements, in the Preamble to the Regulation and in numerous court filings across the United States, that "these regulations are not retroactive," and that the Treasury and IRS "disagree with the characterization of the regulations as retroactive." T.D. 9511, 75 Fed. Reg. at 78898; *see also* Gov't Br. 29.

The decisions by the Tenth Circuit, D.C. Circuit, and Federal Circuit — applying the Regulation in similar circumstances notwithstanding the plain language of the effective date — were wrongly decided and should not be followed.[8] The Appeals Court in each case made the same fatal misstep. Each court failed to test the assumption upon which the Government's "interpretation" of the effective date is based — that the litigation had the legal effect of suspending the limitations period.[9] This assumption is false where, as here, the IRS did not timely issue the FPAA, which is a prerequisite to triggering the suspension rules.

---

[8] *See Intermountain Ins. Svc. of Vail v. Comm'r*, 650 F.3d 691 (D.C. Cir. Jun. 21, 2011), *petition for cert. filed*, No. 11-663 (U.S. Nov. 16, 2011); *Salman Ranch, Ltd. v. Comm'r*, 647 F.3d 929 (10th Cir. May 31, 2011), *petition for cert. filed*, No. 11-582 (U.S. Nov. 7, 2011); *Grapevine Imports, Ltd. v. United States*, 636 F.3d 1368 (Fed. Cir. Mar. 11, 2011), *petition for cert. filed*, No. 11-163 (U.S. Aug. 5, 2011).

[9] *See Intermountain*, 650 F.3d at 707-09; *Salman Ranch*, 647 F.3d at 941-42; *Grapevine Imports*, 636 F.3d at 1382-83.

3. THE REGULATION IS NOT RETROACTIVE AND CANNOT BE APPLIED RETROACTIVELY.

The Government urges this Court that the Regulation could apply retroactively. Gov't Br. 42-43. The obvious flaw with this argument is that the Regulation is not retroactive. The Treasury issued the Regulation with a contemporaneous effective date, and stated unequivocally in the Preamble that "these regulations are not retroactive." The Preamble further stated that Treasury and the IRS "disagree with the characterization of the regulations as retroactive." T.D. 9511, 75 Fed. Reg. at 78898. The Government has maintained this position in dozens of cases, including the case before this Court. Gov't Br. 29.

While I.R.C. § 7805(b) states that regulations are presumed retroactive unless otherwise proscribed, the Government has "otherwise proscribed" in the Regulation. I.R.C. § 7805 does not authorize the Treasury "to add retroactive effect that a Regulation would otherwise not have." *See Agway, Inc. v. United States*, 524 F.2d 1194, 1199 (Ct. Cl. 1975) (rejecting the Government's attempt to retroactively apply a rule that specified its own prospective application).

Further, once Treasury promulgates a regulation, its provisions — including effective date — are binding on the Government and taxpayers equally. The Ninth Circuit's decision in *Pacific National Bank v. Commissioner*, 91 F.2d 103 (9th Cir. 1937), is instructive on this point. At issue in that case was a Treasury regulation that raised a presumption of deductibility for bad debts "charged off" in accordance with instructions from federal and state regulatory agencies. The taxpayer deducted the exact amount of

a charge-off made pursuant to the orders of a national bank examiner. The IRS disallowed the deduction, which the Board of Tax Appeals sustained.

The Ninth Circuit reversed on appeal. The court found uncontroverted evidence of the taxpayer's compliance with the regulation, raising the presumption of deductibility that the IRS made no effort to rebut. The Ninth Circuit chastised the Government for its failure to abide by its own regulations:

> The suggestion that Treasury Regulations . . . are binding on taxpayers, but not on the Commissioner or on the Board of Tax Appeals, cannot be entertained. Tax officials and taxpayers alike are under the law, not above it.

Pacific Nat'l Bank, 91 F.2d at 105.

The Government follows a comparable "do as I say, not as I do" approach in its enforcement of the Regulation. Although the Treasury promulgated the Regulation with a contemporaneous effective date, the Government seeks to apply the Regulation retroactively in a manner that re-writes the effective date provision. Under *Pacific National Bank*, for better or worse, the Government is bound by the terms of the Regulation it promulgated. The Regulation therefore cannot apply retroactively.

An additional fatal flaw is that retroactive application of the Regulation produces a legally impermissible result. The Ninth Circuit's decision in *Chenault v. U.S. Postal Service*, 37 F.3d 535 (9th Cir. 1994), illustrates this point and is instructive. The

plaintiff in that case brought discrimination claims against the U.S. Postal Service. The district court dismissed one of the claims as time-barred because it was not brought within the required 30-day period. A few months later, Congress passed legislation that extended the period to 90 days. The plaintiff moved to reinstate its claim, which under the 90-day period, would be timely. Applying this Court's decision in *Landgraf v. USI Film Prods.*, 511 U.S. 244 (1994), the Ninth Circuit held that to apply the new statute of limitations retroactively would "alter the substantive rights" of a party and "increase a party's liability," as the party would be "forced to defend an action that was previously time-barred." *Chenault*, 37 F.3d at 539. In holding that the new statute of limitations could not be applied retroactively, the court stated "a newly enacted statute that lengthens the applicable statute of limitations may not be applied retroactively to revive a plaintiff's claim that was otherwise barred under the old statutory scheme." *Id.*

This Court expressed its approval of *Chenault*'s holding in a case involving the retroactive application of an amendment to the False Claims Act ("FCA"). *See Hughes Aircraft Co. v. United States*, 520 U.S. 939, 950-52 (1997). The FCA permits suits by private parties against anyone who submits a false claim to the government. The provision at issue permitted *qui tam* actions to proceed based on information already in the government's possession. *Id.* at 945-46. The parties agreed that if the amendment did not apply, the plaintiff's claims were barred. *Id.* at 945. In comparing its case to *Chenault*, this Court stated "[t]he [newly-enacted] amendment would revive that action, subjecting [the defendants] to previously foreclosed . . . litigation, much like extending a statute of limitations

after the pre-existing period of limitations has expired impermissibly revives a moribund cause of action." *Id.* at 950 (citing *Chenault*, 37 F.3d at 537, 539).

The Government fails to address *Chenault* and *Hughes Aircraft* and instead analyzes retroactive application of the Regulation based on an abuse-of-discretion standard. *See* Gov't Br. 42-43. This argument should be summarily rejected. Where retroactivity achieves a *legally-prohibited result*, retroactive application is a per se abuse of discretion.

4. APPLYING THE REGULATION CREATES A "HEADS THE GOVERNMENT WINS – TAILS THE TAXPAYER LOSES" SITUATION THAT FRUSTRATES THE PURPOSE BEHIND STATUTES OF LIMITATION.

Adopting the Government's "interpretation" places the taxpayers in *Home Concrete* and similar cases in an impossible, no-win situation at the time they receive the FPAA. Do they challenge the untimely FPAA by filing a court action, and by doing so, allow the Government the opportunity to promulgate regulations to make the FPAA timely and nullify their statute-of-limitations defense? Or do the taxpayers not challenge the FPAA, thereby waiving their statute-of-limitations defense?[10] By virtue of the Regulation, the Government has stripped the taxpayers of their

---

[10] The issue of whether the IRS assessed tax attributable to partnership items within the statute of limitations (i.e., a "statute of limitations defense") is a partnership item that must be raised at the partnership level. *See Weiner v. United States*, 389 F.3d 152, 157 (5th Cir. 2004); *Chimblo v. Comm'r*, 177 F.3d 119, 125 (2d Cir. 1999); *Kaplan v. United States*, 133 F.3d 469, 473 (7th Cir. 1998); *Crowell v. Comm'r*, 102 T.C. 683, 693 (1994).

statutory right to a timely assessment by the IRS and their right to judicial review of both the IRS's determinations and their statute-of-limitations defenses. By taking no action, the taxpayers lose. By challenging the IRS, the taxpayers lose. In every instance, the taxpayers lose. The law simply cannot allow the IRS to penalize taxpayers for exercising the rights expressly granted to them by Congress in the Internal Revenue Code.

To allow the Government's overreaching sets a dangerous precedent. Each time the Government lost in court, it could simply create an administrative fix, i.e., regulation, and apply the fix to ongoing litigation under the guise that the litigation is "not yet final." This would allow the Government to avoid any permanent defeat on a tax issue and seek to displace, at any time, the opinion of the judiciary with its own opinion. Circuit Court Judge Wilkinson warned of such dangers in his concurring opinion to the appeals court decision, characterizing the Government's "interpretation" of the Regulation as "something of an inversion of the universe and to pass the point where the beneficial application of agency expertise gives way to a lack of accountability and a risk of arbitrariness." Pet. App. 20a.

Further, no tax dispute would ever be stale. Should the tax dollars justify it, the Government could simply promulgate a new regulation to resurrect expired claims that are the subject of ongoing litigation. This would thwart the principles of justice and fairness upon which the rules of limitation were founded:

> It probably would be all but intolerable, at least Congress has regarded it as ill-advised, to have

> an income tax system under which there never would come a day of final settlement and which required both the taxpayer and the Government to stand ready forever and a day to produce vouchers, prove events, establish values and recall details of all that goes into an income tax contest. Hence a statute of limitation is an almost indispensable element of fairness as well as of practical administration of an income tax policy.

Rothensies v. Elec. Storage Battery Co., 329 U.S. 296, 301 (1946).

CONCLUSION

The simple truth is that an untimely FPAA does not suspend the limitations period. Once a limitations period has expired, neither the issuance of an FPAA nor subsequent filing of a lawsuit can reopen the period. Likewise, the lack of a final decision does not operate to hold open a limitations period which has already expired. When these simple truths are properly applied here, the result is unequivocally clear: the tax year at issue was closed when the Regulation took effect, and therefore the Regulation does not apply.

Nor can the Regulation apply retroactively. To do so would require this Court to improperly disregard the explicit terms of the Regulation's effective date provision. Further, applying the Regulation retroactively would reopen a closed tax year which impermissibly strips the taxpayer of its substantive rights against an untimely tax assessment. It places the taxpayers in a "Heads the Government Wins, Tails

the Taxpayer Loses" situation, wherein the taxpayers either voluntarily, or by virtue of challenging the IRS, forfeit their statute-of-limitations defenses. For these reasons, the Regulation cannot and should not apply.

Respectfully Submitted,

JOEL N. CROUCH
Counsel of Record
DAVID E. COLMENERO
MEADOWS, COLLIER, REED, COUSINS,
CROUCH & UNGERMAN, L.L.P.
901 Main Street, Suite 3700
Dallas, TX 75202
(214) 744-3700 Telephone
(214) 747-3732 Facsimile
jcrouch@meadowscollier.com

Counsel for Amicus Curiae Daniel S. Burks

Anthony P. Daddino
Texas State Bar No. 24036434
MEADOWS, COLLIER, REED, COUSINS,
CROUCH & UNGERMAN, L.L.P.
901 Main Street, Suite 3700
Dallas, TX 75202
(214) 744-3700 Telephone
(214) 747-3732 Facsimile
adaddino@meadowscollier.com

Counsel for Amicus Curiae Reynolds Properties, L.P.

AMICUS CURIAE BRIEF

No. 11-139

IN THE

Supreme Court of the United States

UNITED STATES OF AMERICA,

Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF OF GRAPEVINE IMPORTS, LTD. AS *AMICUS CURIAE* SUPPORTING RESPONDENTS

HOWARD R. RUBIN
Counsel of Record
ROBERT T. SMITH
KATTEN MUCHIN ROSENMAN LLP
2900 K Street, NW
North Tower – Suite 200
Washington, DC 20007
howard.rubin@kattenlaw.com
202-625-3500

Counsel for Grapevine Imports, Ltd.

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

INTEREST OF *AMICUS CURIAE* 1

SUMMARY OF THE ARGUMENT 4

ARGUMENT 6

THE IRS MAY NOT INVOKE ITS RULEMAKING AUTHORITY TO MANIPULATE THE OUTCOME OF CASES TO WHICH IT IS A PARTY 6

A. The IRS's Attempt to Invoke the Rulemaking Process to Manipulate Pending Tax Cases Represents a Dangerous Consolidation of Legislative, Executive, and Judicial Functions, and Constitutes an Abuse of Discretion 6

B. The Invocation of Newly-Promulgated Regulations, During the Course of Litigation to Which the Promulgating Agency is a Party, Amounts to an Unacceptable Level of Interference with the Independence of the Judiciary 14

C. The IRS's Claimed Authority is Contrary to the Scheme Congress Enacted to Resolve Taxpayer Disputes 22

CONCLUSION 26

TABLE OF AUTHORITIES

CASES

Auer v. *Robbins*,
519 U.S. 452 (1996) 12

Bowen v. *Georgetown Univ. Hosp.*,
488 U.S. 204 (1988) 7

Burks v. *United States*,
633 F.3d 347 (5th Cir. 2011)
petition for cert. filed, 80 U.S.L.W. 3090
(U.S. Aug. 11, 2011) (No. 11-178) 8, 12

Caterpillar Tractor Co. v. *United States*,
589 F.2d 1040 (Ct. Cl. 1978) 8

Chock Full O' Nuts Corp. v. *United States*,
453 F.2d 300 (2d Cir. 1971) 7, 8

Colony, Inc. v. *Comm'r*,
357 U.S. 28 (1958) 2, 8, 18, 19

Freytag v. *Comm'r*,
501 U.S. 868 (1991) 4, 21, 24

Glidden Co. v. *Zdanok*,
370 U.S. 530 (1962) 24

Grapevine Imports, Ltd. v. *United States*,
636 F.3d 1368 (Fed. Cir. 2011),
petition for cert. filed, 80 U.S.L.W. 3090
(U.S. Aug. 5, 2011) (No. 11-163) 2, 9, 10, 18, 21

Hayburn's Case,
2 U.S. (2 Dall.) 408 (1792) 16, 18, 22

Home Concrete & Supply, LLC v. *United States*,
634 F.3d 249 (4th Cir.),
cert. granted, 132 S. Ct. 71 (2011) 13

Lampf, Pleva, Lipkind, Prupis & Petigrow v.
Gilbertson, 501 U.S. 350 (1991) 17

Mayo Found. for Med. Educ. v. *United States*,
131 S. Ct. 704 (2011) 10, 11, 12

Nat'l Cable & Telecomms. Ass'n v. *Brand X*
Internet Servs., 545 U.S. 967 (2005) 19, 20

Plaut v. *Spendthrift Farm, Inc.*,
514 U.S. 211 (1995) ..... *passim*

Salman Ranch, Ltd. v. *United States*,
573 F.3d 1362 (Fed. Cir. 2009) 2, 9, 21

Smiley v. *Citibank (South Dakota), N.A.*,
517 U.S. 735 (1996) 10, 11

Talk Am., Inc. v. *Mich. Bell Tel. Co.*,
131 S. Ct. 2254 (2011) 12, 13

Tallahassee Mem'l Reg'l Med. Ctr. v. *Bowen*,
815 F.2d 1435 (11th Cir. 1987),
cert. denied, 485 U.S. 1020 (1988) 8

United States v. *Klein*,
80 U.S. (13 Wall.) 128 (1872) 15, 16, 21

United States v. *Morton*,
467 U.S. 822 (1984) 9, 10

United States v. *Padelford*,
76 U.S. (9 Wall.) 531 (1869) 15

STATUTES

26 U.S.C. § 6501(e)(1)(a) 1, 2
26 U.S.C. § 6226(a) 22
26 U.S.C. § 6226(f) 5, 23, 24
26 U.S.C. § 6226(g) 23
26 U.S.C. § 6229(c)(2) 1
26 U.S.C. § 7441 24
26 U.S.C. § 7443(b) 24
28 U.S.C. § 1491 23

OTHER AUTHORITIES

A. Bickel, *The Least Dangerous Branch* (1962) 19

Federalist Papers (G. Willis ed. 1982) 4, 5, 6, 7, 20

IRS Notice 2000-44,
2000-36 I.R.B. 255 (Sept. 4, 2000) 8

Montesquieu, *Spirit of Laws* bk. XI
(O Piest ed., T. Nugent transl. 1949) 13

Petition for a Writ of Certiorari,
Grapevine Imports, Ltd. v. *United States*,
No. 11-163 (U.S. Aug. 5, 2011) 9

S. Rep. No. 97-275 (1981),
reprinted in 1982 U.S.C.C.A.N. 11 23

INTEREST OF *AMICUS CURIAE*

Grapevine Imports, Ltd. is a party to a related petition pending before this Court, *Grapevine Imports, Ltd.* v. *United States*, No. 11-163, which presents the same fundamental issues that are presented in this case. As such, Grapevine Imports, Ltd. and its tax matters partner, T-Tech, Inc. (collectively, "Grapevine"), have a substantial interest in the resolution of the issues before the Court in this case.[1]

Like Respondents here, Grapevine filed suit against the government, challenging a more-than-three-year-old adjusted tax assessment as untimely. And in like manner, Grapevine argued that the government could not avail itself of the Internal Revenue Code's extended statute of limitations, 26 U.S.C. §§ 6229(c)(2), 6501(e)(1)(A), because an overstatement of basis does not constitute an omission from gross income. Finally, just like here, the government countered Grapevine's suit by promulgating regulations, which it claims alter the outcome not only of future cases, but also of pending cases in which the government is a party.

Even assuming that Congress did not speak to the precise question at issue here, the level to which the government contends an agency may manipulate a judicial proceeding is on stark display in this case.

---

[1] Counsel for all parties have consented to the filing of this brief, and those consents are on file with the Clerk of the Court. No counsel for a party in this case authored this brief in whole or in part. No person or entity—other than Grapevine, its partners, or its counsel—made a monetary contribution specifically for the preparation or submission of this brief.

Despite submitting to the courts' jurisdiction for more than three years unaided by whatever regulatory authority that the IRS purports to possess, the government now claims that the courts essentially have no role in this case other than to adopt the IRS's novel and expansive interpretation of the extended statute of limitations, thereby compelling the courts to enter judgment in the government's favor.

And yet, Grapevine's case presents an even more disturbing example of the level of manipulation that the government argues an agency may exert over judicial proceedings. Unlike here, Grapevine had secured from the trial court a judgment in its favor, and it defended that judgment on appeal in a circuit that had held—consistent with *Colony, Inc.* v. *Commissioner*, 357 U.S. 28 (1958)—that the extended statute of limitations at issue here, 26 U.S.C. § 6501(e)(1)(A), does not apply to an overstatement of basis. *See Salman Ranch, Ltd.* v. *United States*, 573 F.3d 1362 (Fed. Cir. 2009). In Grapevine's case, the government was not deterred—not by an unfavorable trial-court judgment, not even by Supreme Court and circuit-level precedent rejecting the IRS's interpretation. Instead, the government argued for the first time on appeal—and the Federal Circuit agreed—that the IRS could use regulations that were promulgated more than a year after the IRS filed its appeal in the Federal Circuit to reverse the judgment that the Court of Federal Claims had entered in Grapevine's favor. *See Grapevine Imports, Ltd.* v. *United States*, 636 F.3d 1368, 1374-75, 1383-84 (Fed. Cir. 2011), *petition for cert. filed*, 80 U.S.L.W. 3090 (U.S. Aug. 5, 2011) (No. 11-163).

The government's position in both this case and Grapevine's raises serious separation-of-powers concerns, and if adopted, it will have a deleterious effect on the public's confidence in the courts. Make no mistake, the government is arguing that the IRS is empowered to wield the powers associated with all three branches of government—legislative, executive, and judicial—at the same time. According to the government, during the course of litigating specific taxpayer disputes, the IRS may invoke its rulemaking authority to dictate the outcome of specific cases to which it is a party, including lower court decisions entered against it.

If a court may be compelled by regulation to adopt the government's position in a case to which the government is a party, then the executive's encroachment on the judicial power is all the more offensive, because a party to the litigation is co-opting the judiciary to enforce that party's dictates. What is more, such power wielded by a litigant undermines Congress's scheme of empowering courts to resolve taxpayer disputes, and worse still, it threatens to undermine the public's confidence in the courts as independent arbiters of those disputes. Adopting the government's position would render the more than three years that Grapevine spent litigating in the Court of Federal Claims an utter waste of time and money. And it would serve as a powerful disincentive for private parties to litigate even the most legitimate tax grievances against the government.

At bottom, if the IRS is permitted to use its regulatory authority to manipulate the outcome of this case, it will undoubtedly invoke that authority to

Grapevine's detriment—and to the detriment of other private parties who find themselves litigating against governmental agencies. Accordingly, Grapevine submits this brief as *amicus curiae* in support of Respondents.

SUMMARY OF ARGUMENT

"The leading Framers of our Constitution viewed the principle of separation of powers as the central guarantee of a just government." *Freytag* v. *Comm'r*, 501 U.S. 868, 870 (1991). As James Madison explained: "No political truth is certainly of greater intrinsic value or is stamped with the authority of more enlightened patrons of liberty." The Federalist No. 47, at 244 (G. Willis ed. 1982). And in keeping with this truth, the Framers imbued in our Constitution its greatest structural safeguard—"that the power properly belonging to one of the departments[] ought not to be directly and comple[tely] administered by either of the other departments." The Federalist No. 48, at 250.

In the present case, the government is claiming for the executive precisely the kind of consolidated power condemned by our Constitution. According to the government, the IRS may invoke its rulemaking authority during the course of litigating specific tax cases and then use that delegated legislative authority to dictate the outcome of those cases, including in cases—like Grapevine's—in which the IRS had lost in a lower court.

There are at least three problems with this argument. *First*, the power that the executive is claiming here represents a dangerous accumulation of the

three powers of government. The IRS is claiming the authority to serve as legislator, prosecutor, and adjudicator—all at once—through the promulgation of retroactive regulations meant to *enlarge* a statute that Congress enacted to *limit* the IRS's authority to enforce the tax code. According to the Framers, this is the very "definition of tyranny"—where "'the same monarch or senate should enact tyrannical laws, to execute them in a tyrannical manner.'" The Federalist No. 47, at 244, 246 (G. Willis ed. 1982) (J. Madison) (quoting Montesquieu).

Second, the power that the executive is claiming here interferes with the structural independence of the judiciary. According to the government, even after the executive has submitted to the jurisdiction of an independent judiciary, it may invoke its rulemaking authority to compel the judiciary to rule in its favor. Although this Court has only had occasion to address *congressional enactments* that interfere with the independence of the judiciary, *see, e.g.*, *Plaut* v. *Spendthrift Farm, Inc.*, 514 U.S. 211, 218-19 (1995), unilateral compulsion by the executive is just as offensive to the Constitution.

Third, the power claimed here is contrary to the statutory scheme that Congress enacted for the resolution of taxpayer disputes. As part of that scheme, Congress vested in independent tribunals, not beholden to the executive, the authority to decide the precise substantive dispute at issue here. *See* 26 U.S.C. § 6226(f). The IRS is plainly attempting to circumvent this statutory scheme when, as a party to litigation, it claims for itself the authority to declare what the law is in that very case. Nor can the IRS

defend its conduct based on its authority to issue rules of general applicability. Whatever regulatory authority Congress has vested in the IRS, that general grant must give way to Congress's specific judicial-review scheme—one that did not cede to the executive the power to decide individual taxpayer disputes.

ARGUMENT

THE IRS MAY NOT INVOKE ITS RULEMAKING AUTHORITY TO MANIPULATE THE OUTCOME OF CASES TO WHICH IT IS A PARTY.

A. The IRS's Attempt to Invoke the Rulemaking Process to Manipulate Pending Tax Cases Represents a Dangerous Consolidation of Legislative, Executive, and Judicial Functions, and Constitutes an Abuse of Discretion.

To the Framers of our Constitution, separating the powers of government was a means to prevent a potentially deleterious end: The "accumulation of all powers, legislative, executive, and judicial, in the same hands." The Federalist No. 47, at 244 (G. Willis ed. 1982) (J. Madison). According to Thomas Jefferson: "The concentrati[on of these powers] in the same hands[] is precisely the definition of despotic government." The Federalist No. 48, at 252 (J. Madison quoting T. Jefferson). And James Madison—associating any such accumulation with "tyranny"—rejected the notion that our federal Constitution is "chargeable with the accumulation of power or with a mixture of powers having a dangerous ten-

dency to such an accumulation." The Federalist No. 47, at 244.

In the present case, the government is claiming for the executive precisely the kind of consolidated power condemned by our Constitution. According to the government, the IRS may invoke its rulemaking authority (a delegation of Congress's legislative function) during the course of litigating specific tax cases (an exercise of the IRS's executive authority) and use its delegated legislative authority to dictate the outcome of specific cases to which it is a party (an obvious exercise of judicial power).

Although this Court has never decided the propriety of an agency using its rulemaking authority to manipulate the outcome of pending cases to which the government is a party, this Court has condemned efforts by agency counsel to cloak their legal arguments in the deference that is normally reserved for formal agency rulemaking. In *Bowen* v. *Georgetown University Hospital*, the Court explained that "[d]eference to what appears to be nothing more than an agency's convenient litigation position" is "entirely inappropriate." 488 U.S. 204, 213 (1988).

The lower federal courts, however, have confronted this situation, and for many years they had been near universal in condemning the precise argument the government advances here. Beginning in *Chock Full O' Nuts Corp.* v. *United States*, a tax dispute, the Second Circuit explained that the IRS "may not take advantage of [its] power to promulgate retroactive regulations during the course of a litigation for the purpose of providing [itself] with a defense based on the presumption of validity accorded

to such regulations." 453 F.2d 300, 303 (2d Cir. 1971). Other courts have followed suit—including in a case similar to the one at issue here, *Burks* v. *United States*, 633 F.3d 347, 360 n.9 (5th Cir. 2011) (explaining that, even if *Colony* is not controlling, it is not clear that deference is owed in a "situation where, during the pendency of suit, the [IRS] promulgated determinative retroactive regulations" displacing "prior adverse judicial decisions on the identical legal issue"), *petition for cert. filed*, 80 U.S.L.W. 3090 (U.S. Aug. 11, 2011) (No. 11-178); *see also Caterpillar Tractor Co.* v. *United States*, 589 F.2d 1040, 1043 (Ct. Cl. 1978) (quoting *Chock Full O' Nuts*). And still other courts have concluded that such action is an abuse of agency discretion. *See, e.g.*, *Tallahassee Mem'l Reg'l Med. Ctr.* v. *Bowen*, 815 F.2d 1435, 1452, 1456 (11th Cir. 1987) (holding that the issuance of regulations in an attempt to moot an adverse trial-court judgment in a case where the agency is a party is an "abuse of the interaction between administrative agencies and the courts" and an "abuse [of] the litigation process"), *cert. denied*, 485 U.S. 1020 (1988). Regardless of how it is categorized, the power claimed for the IRS here represents a dangerous consolidation of governmental functions, one that is rife with abuse.

In fact, the IRS has already engaged in abusive conduct in these very cases. Having failed to give prior notice that it considered the substantive transaction at issue here not properly allowable under the tax code, the IRS issued a notice that purported to have retroactive effect. *See* IRS Notice 2000-44, 2000-36 I.R.B. 255 (Sept. 4, 2000). Thereafter, the IRS argued, for the first time in roughly fifty years,

that *Colony* did not preclude the agency from availing itself of the Internal Revenue Code's extended statute of limitations. Still, the IRS did not exercise its rulemaking authority, even after the courts began to reject its incorrect interpretation of *Colony*. Only after it suffered set backs in the two federal appellate courts to consider the issue did the IRS promulgate regulations purporting to overrule the growing number of cases (in the trial and appellate courts) that were rejecting its position. In *Grapevine* in particular, the IRS waited more than three years—and after it had lost in the trial court—before promulgating the regulations at issue here.[2]

In an attempt to defend the IRS's authority to manipulate the judicial process, the government argues that this Court "[c]onfront[ed] exactly th[is] scenario in *United States* v. *Morton*, 467 U.S. 822 (1984)," and implies that *Morton* held that an

---

[2] Even more troubling, the government—in opposing a motion by Grapevine to consolidate its appeal with a related case, *Salman Ranch, Ltd.* v. *United States*, No. 2008-5053 (Fed. Cir.)—argued to the Federal Circuit that Grapevine's case should be stayed, because Grapevine might have the benefit of a favorable decision in *Salman Ranch*. *See Grapevine*, 636 F.3d at 1374. Rather than honor that representation, however, the IRS promulgated the regulations at issue here after the Federal Circuit handed the taxpayers a victory in *Salman Ranch*, *see* 573 F.3d at 1377, and then argued that the regulations deprived Grapevine of the benefit of that decision, *Grapevine*, 636 F.3d at 1374-75. *See also* Petition for a Writ of Certiorari at 7-10, *Grapevine Imports, Ltd.* v. *United States*, No. 11-163 (U.S. Aug. 5, 2011). By applying to Grapevine's case the newly-promulgated, made-for-litigation regulations, the Federal Circuit blessed the IRS's bait and switch, thereby rendering meaningless the three years of litigation in which the government and Grapevine had engaged up to that point in time.

agency's status as a party has no bearing on whether the agency may invoke its rulemaking authority in pending litigation. U.S. Br. at 40. But *Morton* stands for no such proposition.

In *Morton*, this Court did not hold that an agency may reverse an adverse judgment by regulation or otherwise manipulate the judicial process. To the contrary, the opinion in *Morton* makes clear that this Court was compelled to reverse the lower courts' decisions—and rule in the government's favor—based on the "plain language of the statute." 467 U.S. at 826-29. After reaching that conclusion (one that is fully consistent with *Chevron*'s first step), the Court went on to observe that regulations, issued after the lower courts issued their decisions, provided *further support* for the Court's interpretation of "the plain language of the statute." *Id.* at 836.

To be sure, the Court also observed in a footnote that it found inconsequential the fact that the regulations at issue were not promulgated "until after [the] suit was brought." *Id.* at 835 n.21. But this is clear *dicta*. The Court did not consider, let alone decide, any of the issues presented here. Thus, *Morton*'s holding falls well short of establishing that an agency may use new regulations to compel an appellate court to adopt its litigating position or, as occurred in *Grapevine*, reverse what otherwise would have been a loss for the government.

The government also defends the IRS's authority to manipulate the judicial process by quoting out of context certain statements that this Court made in *Smiley* v. *Citibank (South Dakota), N.A.*, 517 U.S. 735 (1996), and *Mayo Foundation for Medical Educa-*

tion v. *United States*, 131 S. Ct. 704 (2011). *See* U.S. Br. at 40. But neither case held that an agency may use its rulemaking authority to achieve the result the government is seeking here.

In *Smiley*, the government was not even a party to the case, and as a result, this Court had no occasion to address the issues presented here. 517 U.S. at 737-38. Thus, at most, *Smiley* stands for a completely unrelated and far more limited proposition—that, in a case where an agency is *not a party* to litigation, a court may defer to a regulation even though that regulation was prompted by a problem that was identified in that very litigation. *Id.* at 741. In such a situation, however, the agency is not using its rulemaking authority to snatch for itself victory from the jaws of judicial defeat; rather, it is addressing a problem identified by private parties that Congress intended for that agency to resolve. *See id.* at 740-41. Moreover, in that situation, the agency is wearing but one hat—that of delegated lawmaker.

Similarly, *Mayo Foundation* did not address the central issues presented herein. As the Court in *Mayo Foundation* explained, the lawsuit underlying the Mayo Foundation's appeal was filed "*[a]fter*" the IRS promulgated the regulations at issue in that case. 131 S. Ct. at 710 (emphasis added). Thus, contrary to the government's assertion, *Mayo Foundation* could not have addressed an agency's ability to invoke its rulemaking authority to manipulate the outcome of pending cases in which the agency is a party. U.S. Br. at 40 (quoting out of context *Mayo Found.*). Rather, *Mayo Foundation* noted, consistent with *Smiley*, that if the government is seeking to ap-

ply a regulation on a *prospective* basis in a *subsequent* case, then it is immaterial that *prior* litigation identified a problem that the agency sought to resolve through the promulgation of those regulations. *See also Burks*, 633 F.3d at 360 (explaining that *Mayo Foundation* did not involve a situation where, "during the pendency of suit, the treasury promulgated determinative, retroactive regulations [in the wake of] prior adverse judicial decisions on the identical legal issue").

Finally, even if the government could somehow transform these inapposite statements and *dicta* into authoritative holdings of this Court, those transformed holdings would warrant reexamination. Just last Term, Justice Scalia correctly called for the reexamination of an otherwise settled principle of administrative law—that courts should defer to an agency's interpretation of its own regulations, *see, e.g.*, *Auer* v. *Robbins*, 519 U.S. 452, 461 (1996)—because that principle was imbued with separation-of-powers concerns. *See Talk Am., Inc.* v. *Mich. Bell Tel. Co.*, 131 S. Ct. 2254, 2266 (2011) (Scalia, J., concurring). As Justice Scalia explained:

> It seems contrary to fundamental principles of separation of powers to permit the person who promulgates a law to interpret it as well. "When the legislative and executive powers are united in the same person, or in the same body of magistrates, there can be no liberty; because apprehensions may arise, lest the same monarch or senate should enact tyrannical laws, to execute them in a tyrannical manner."

Id. (quoting Montesquieu, *Spirit of Laws* bk. XI, ch. 6, at 151-52 (O Piest ed., T. Nugent transl. 1949)). Moreover, Justice Scalia properly noted that "deferring to an agency's interpretation of its own rule encourages the agency to enact vague rules which give it the power, in future adjudications, to do what it pleases," which thereby "frustrates the notice and predictability purposes of rulemaking, and promotes arbitrary government." *Id.*

Even greater concerns are at play here. The IRS has not waited until "future adjudications" to invoke its interpretation. Rather, it has claimed for itself the authority to serve as legislator, prosecutor, and adjudicator—all at once—through the promulgation of *retroactive* regulations meant to enlarge a statute that Congress enacted for the exact opposite purpose—to limit the IRS's authority to proceed against taxpayers.

At every turn of these cases, the IRS has used its rulemaking authority in a manner that can only be classified as "arbitrary" and abusive. *Talk Am.*, 131 S. Ct. at 2266 (Scalia, J., concurring). As Judge Wilkinson explained below, what the IRS seeks to do here threatens to "disrupt[]" the "balance" of power between courts and agencies, and presents "a lack of accountability and a risk of arbitrariness." *Home Concrete & Supply, LLC* v. *United States*, 634 F.3d 249, 259-60 (4th Cir.) (Wilkinson, J., concurring), *cert. granted*, 132 S. Ct. 71 (2011). At the very least, the IRS's efforts in this case to wield the powers associated with all three branches of government should be set aside as arbitrary and capricious.

B. The Invocation of Newly-Promulgated Regulations, During the Course of Litigation to Which the Promulgating Agency is a Party, Amounts to an Unacceptable Level of Interference with the Independence of the Judiciary.

The government's position here also would amount to a serious invasion of the structural independence of the judiciary. According to the government, even after the executive has submitted to the jurisdiction of an independent judiciary, the executive nevertheless may invoke its rulemaking authority to compel the judiciary to rule in its favor.

In *Plaut* v. *Spendthrift Farm, Inc.*, this Court identified three categories of legislation "that require federal courts to exercise the judicial power in a manner that Article III forbids." 514 U.S. 211, 218 (1995). Although these forms of interference differ from the form of interference at issue here—the types of offensive conduct identified in *Spendthrift Farm* all involved *congressional enactments*, whereas here, the conduct is embodied in *unilateral executive action*—the result is the same: What another branch seeks to do here is repugnant to the independence of the judiciary. Indeed, there are significant parallels between the authority that the executive is claiming here for itself and the offensive enactments that this Court discussed in *Spendthrift Farm*. Moreover, because an agency's rulemaking authority exists by the grace of Congress, that agency cannot claim to have *more* authority than Congress to interfere with the affairs of the judiciary.

The first type of offensive enactment indentified by this Court in *Spendthrift Farm* arose in *United States* v. *Klein*, 80 U.S. (13 Wall.) 128 (1872). In that case, the Court wrestled with "a statute that was said '[to] prescribe rules of decision to the Judicial Department of the government in cases pending before it.'" *Spendthrift Farm*, 514 U.S. at 218 (quoting *Klein*, 80 U.S. at 146). The statute at issue provided that individuals whose property was seized during the Civil War could recover that property, or receive compensation for it, upon proof to the Court of Claims that they had remained loyal to the Union. In *Klein*, the claimant had received a presidential pardon, which this Court had previously held must be treated as conclusive proof of loyalty, *see United States* v. *Padelford*, 76 U.S. (9 Wall.) 531 (1869). As a result, the Court of Claims ordered judgment on that basis. The United States then appealed that judgment to this Court. While that appeal was pending, Congress enacted legislation providing that a pardon was inadmissible as proof in support of a claim; that a pardon, without an express disclaimer of guilt, was presumptive proof of *disloyalty*; and that the courts, including the Supreme Court, must dismiss for want of jurisdiction any pending claims based on a pardon. *See Klein*, 80 U.S. at 129.

This Court held the supervening statute unconstitutional and affirmed the judgment of the Court of Claims. *Id.* at 146-48. In the process, the Court questioned the power of Congress to "prescribe rules of decision to the Judicial Department of the government in cases pending before it"—a rule designed to resolve "a cause in a particular way," *id.* at 146—and explained that Congress may not effectively di-

rect the reversal of a decision because that "decision, in accordance with settled law, must be adverse to the government and favorable to the suitor," *id.* at 147.

The second type of unconstitutional interference—according to the Court in *Spendthrift Farm*—is "exemplified" by *Hayburn's Case*, 2 U.S. (2 Dall.) 408 (1792), which "stands for the principle that Congress cannot vest review of the decisions of Article III courts in officials of the Executive Branch," *Spendthrift*, 514 U.S. at 218. In *Hayburn's Case*, five of the six Supreme Court justices, serving at the time on the regional circuit courts, found unconstitutional an act that directed the judges of those courts to determine whether veterans of the Revolutionary War qualified for a pension, but which permitted the Secretary of War to refuse to follow the courts' recommendations. 2 U.S. at 408-10 & n.*. As the justices explained in a series of opinions reported in *Hayburn's Case*, such revision and control is "radically inconsistent with the independence of [the] judicial power which is vested in the courts." *E.g.*, *id.* at 410 n.* (Wilson and Blair, J.J.); *see also id.* (Iredell, J.) (explaining that the act "subjects the decision of the court to a mode of revision which we consider to be unwarranted by the Constitution").

The third type of unconstitutional interference was identified for the first time in *Spendthrift Farm* itself. As the Court explained, "only courts [were] involved" in the application of the legislation at issue in *Spendthrift Farm*, whereas in the earlier-discussed cases, there was some executive involvement. 514 U.S. at 218. Thus, the Court went on to

identify a third category of legislation that offends the Constitution: legislation that requires the "federal courts to exercise '[t]he judicial Power of the United States' in a manner repugnant to the text, structure, and traditions of Article III." *Id.* at 217 (citation omitted).

In *Spendthrift Farm*, a lower court had dismissed with prejudice a prior action between the parties involving allegations of securities fraud. The lower court deemed the plaintiff's prior action untimely under this Court's then-recent interpretation of the applicable statute of limitations in *Lampf, Pleva, Lipkind, Prupis & Petigrow* v. *Gilbertson*, 501 U.S. 350 (1991). Congress responded by adopting legislation authorizing litigants who were aggrieved under *Lampf* to file a motion to reinstate any action previously dismissed with prejudice. *See Spendthrift Farm*, 514 U.S. at 213-15. Thereafter, the plaintiffs in *Spendthrift Farm* attempted to avail themselves of the new law, but the lower courts refused.

On appeal, this Court affirmed the lower courts' denial of reinstatement on the ground that the law required federal courts to exercise the judicial power in a manner repugnant to Article III. As the Court explained, once a judgment achieves finality, it "becomes the last word of the judicial department with regard to a particular case or controversy, and Congress may not declare by retroactive legislation that the law applicable *to that very case* was something other than what the courts said it was." *Id.* at 227.

Here, the source of interference is slightly different than those discussed in *Spendthrift Farm*, but it is impermissible interference nonetheless: The ex-

ecutive is unilaterally invoking a general grant of rulemaking authority to dictate the outcome of pending cases to which it is a party. If anything, the interference at issue here is more offensive than that discussed in *Spendthrift Farm*, because the executive is acting without express authorization from Congress. *Cf. Hayburn's Case*, 2 U.S. at 408-10 & n.* (striking down a statutory scheme that expressly authorized the executive to sit in review of the judiciary).

To be sure, *Spendthrift Farm* was decided on principles of finality (once all appeals are exhausted, the judgment embodies the final word of the judicial department on a given case or controversy), whereas here and in *Grapevine*, the parties have not yet exhausted the appeals process. Thus, *Spendthrift Farm* acknowledges that "*Congress* can always revise the judgments of Article III courts in one sense: When a new law makes clear that it is retroactive, an appellate court must apply that law in reviewing judgments still on appeal that were rendered before the law was enacted, and must alter the outcome accordingly." 514 U.S. at 226 (emphasis added).

In the present case, however, the government is not requesting that the Court honor its obligation to apply for the first time on appeal a new enactment of Congress. Quite the opposite. Congress has not amended the statute at issue in any meaningful sense since this Court decided *Colony* more than a half century ago. *See* Resp. Br. at 5-9.

Instead, the government is arguing that this Court must defer to unilateral executive action compelling the judicial department to achieve the execu-

tive's ends. Indeed, in this very case, the government is arguing that this Court must defer to an interpretation advanced by a party to the litigation, involving a statute designed to limit that party's authority—without any direction from Congress, and involving an interpretation contrary to Congress's clear intent.

In a situation such as this one, an agency may not manipulate the outcome of pending cases simply because the appeals process has not yet been exhausted. After all, "the finality or lack of it in judicial judgments is rather a matter of degree." Alexander Bickel, *The Least Dangerous Branch* 117 (1962). Under strict adherence to principles of finality, an agency could overrule a decision of this Court by promulgating contrary regulations *after* this Court entered its decision, but before the matter was committed to the lower court for the entry of a final judgment. Thus, an agency's authority to promulgate rules of general effect must give way to a more important interest: the judiciary's independence from compelled manipulation by a party to litigation.

Indeed, this Court has strongly suggested that, absent express congressional direction, agencies may not use their rulemaking authority to manipulate the judicial process. *See Nat'l Cable & Telecomms. Ass'n* v. *Brand X Internet Servs.*, 545 U.S. 967, 983 (2005) (emphasizing that judicial decisions may not be "revers[ed] by executive officers"); *see also id.* at 1016-17 (Scalia, J., dissenting). In *Brand X*, this Court held that FCC regulations, which were contrary to a *previous* judicial interpretation of an ambiguous statute, were entitled to deference, but only in *subsequent*

litigation. *Id.* at 982-84. Importantly, in responding to Justice Scalia's criticism that the Court's holding effectively allowed the executive department to "revise[], over-turn[], or refuse[]" to give full faith and credit to judgments of the judicial department, 545 U.S. at 1017 (Scalia, J., dissenting), the Court was adamant that its holding did not amount to such a troubling result. In particular, the Court emphasized that by requiring courts to give deference to an agency's "decision to construe a[n ambiguous] statute differently from a court" in a *subsequent* case, the Court was not announcing a rule that subjected current or prior judicial decisions to reversal by executive officers. *See id.* at 983.

The level of manipulation here amounts to such a reversal. Moreover, such a finding does not call into question the continued validity of *Brand X*. Under *Brand X*, an agency may promulgate regulations—even regulations that are contrary to a prior judicial interpretation of an ambiguous statute—but the agency may only invoke that regulation on a *prospective* basis, and only in *subsequent* litigation. *See* 545 U.S. at 982-84.

The government's contrary position, if adopted, will undermine the independence of the judiciary in the eyes of the public, and weaken the institutional clout upon which the judiciary relies to ensure the enforcement of its judgments. After all, the judiciary is wholly dependent on the executive to enforce its judgments. *See, e.g.*, The Federalist No. 78, at 394 (G. Willis ed. 1982) (A. Hamilton) (explaining that the judiciary "may truly be said to have neither Force nor Will, but merely judgment; and must ulti-

mately depend upon the aid of the executive arm even for the efficacy of its judgments"). Litigants will not bring suits in courts involving the government if the executive is viewed as pulling the strings, and the executive has no incentive to respect the authority of the judiciary to render decisions adverse to it if the executive can achieve during the pendency of litigation a result that a court would not otherwise award to it. That is precisely what happened to Grapevine, where the government acknowledged that, without application of its newly-minted regulations, it would have lost the case under the Federal Circuit's precedent in *Salman Ranch*. *See Grapevine*, 636 F.3d at 1375.

In the end, unilateral compulsion by the executive in situations where it is a party to litigation is just as offensive to the judiciary as a congressional enactment requiring the judiciary to undo the finality of its judgments. When the executive submits to litigation, it submits to the resolution of that dispute by an independent judiciary. *Cf. Klein*, 80 U.S. at 144 ("It was argued that the right to sue the government in the Court of Claims is a matter of favor; but this seems not entirely accurate. It is as much the duty of the government as of individuals to fulfill its obligations."). No party should be able to dictate the outcome of pending litigation—not even the executive.[3]

---

[3] Although Grapevine litigated in the Court of Federal Claims, rather than an Article III court, the government has not confided its manipulation to legislative courts (which nevertheless exercise "judicial" power, *Freytag*, 501 U.S. at 890-91). The government argues in this very case (which arises from a

C. The IRS's Claimed Authority is Contrary to the Scheme Congress Enacted to Resolve Taxpayer Disputes.

Not only does the executive's unilateral action here infringe upon the independence of the judiciary, but it also infringes upon the statutory scheme that Congress enacted for the resolution of taxpayer disputes. In this sense, the power that the executive defends here is worse than what it claimed for itself in *Hayburn's Case*, because at least in *Hayburn's Case*, the executive was acting at the direction of Congress when it chose to disregard judicial pronouncements. 2 U.S. at 410 n.*. Here, by contrast, the IRS can point to no such express authorization from Congress—and there are, in fact, contrary directions from the legislature.

The statutory scheme enacted by Congress to resolve taxpayer disputes holds no place for executive adjudication. Congress did not empower the Commissioner of Internal Revenue to decide taxpayer disputes, subject to review only for an abuse of discretion. Rather, Congress placed such disputes in the hands of the federal district courts, the Tax Court, and the Court of Federal Claims. *See, e.g.*, 26 U.S.C. § 6226(a). In partnership cases such as this one, each court is empowered to "determine all partnership items of the partnership for the partnership taxable year to which the notice of final partnership administrative adjustment relates, the proper alloca-

---

federal district court) that, even if this Court does not find its arguments persuasive, it *must* adopt them so long as they are not unreasonable. *See* U.S. Br. at 37-40.

tion of such items among the partners, and the applicability of any penalty, addition to tax, or additional amount which relates to an adjustment to a partnership item." *Id.* § 6226(f). Moreover, "[a]ny determination by a court under this section shall have the force and effect of a decision of the Tax Court or a final judgment or decree of the district court or the Court of Federal Claims, as the case may be, and shall be reviewable as such," *id.* § 6226(g), by the courts of appeals and, ultimately, by this Court.

It is beyond question that the courts that Congress vested with the authority to resolve taxpayer disputes—the federal district courts, the Tax Court, and the Court of Federal Claims—are entitled to independence from executive manipulation. The United States District Courts are Article III courts, and their independence from the executive is preordained by that stature. However, the remaining courts (the tax and claims courts), though Article I legislative courts, are likewise imbued by Congress with independence from executive manipulation.

When Congress established the Court of Federal Claims, it intended to establish a "truly independent" tribunal with the power to "enter dispositive orders" and "final judgment[s]" against the United States. S. Rep. No. 97-275, at 8, 22 (1981), *reprinted in* 1982 U.S.C.C.A.N. 11, 18, 32. Indeed, Congress expressly vested in that court "jurisdiction to render judgment upon any claim against the United States." 28 U.S.C. § 1491. It is virtually impossible to imagine how the Court of Federal Claims could exercise such authority if—as the IRS did to Grapevine—the executive is permitted to promulgate rules as a means

of reversing that court's judgments. *Cf. Glidden Co.* v. *Zdanok*, 370 U.S. 530, 554-55 (1962) (explaining that final judgments that were issued by the predecessor of the Court of Federal Claims, the Court of Claims, were not subject to "executive revision").

Even the Tax Court is an independent, "Article I legislative court," exercising "judicial, rather than executive, legislative, or administrative, power." *Freytag*, 501 U.S. at 890-91; *see also* 26 U.S.C. § 7441. The judges are not beholden to the Commissioner of Internal Revenue, but rather, are appointed independently by the President and confirmed, on advice and consent, by the Senate. 26 U.S.C. § 7443(b). More importantly, the decisions of the Tax Court "are not subject to review by either the Congress or the President." *Freytag*, 501 U.S. at 891. Thus, "[t]he Tax Court remains independent of the Executive and Legislative Branches." *Id.*

The upshot of all of this is that Congress vested in independent tribunals, not beholden to the executive, the authority to decide the precise substantive dispute at issue here. *See* 26 U.S.C. § 6226(f). The IRS is plainly attempting to circumvent this statutory scheme when, as a party to litigation before these courts, it claims for itself the authority to declare what the law is in those very cases.

Nor can the IRS defend its conduct here based on its authority to issue rules of general applicability. Whatever the IRS's authority to expand a statute of limitation designed to inhibit the IRS from enforcing stale tax assessments, that general grant of rulemaking authority must give way to Congress's specific

judicial-review scheme—one that left the executive powerless to decide individual tax disputes.

Moreover, unlike a "*general statute*," which "may reduce the perception that legislative interference with judicial judgments was prompted by individual favoritism," *Spendthrift Farm*, 514 U.S. at 228 (emphasis added), here the executive cannot escape the charge that it has availed itself of its general regulatory authority to favor itself in cases pending against it. In the end, such party-sponsored manipulation would render impotent the power Congress vested in the courts to decide taxpayer disputes.

Finally, even putting to one side the IRS's structural assault on the judicial-review process enacted by Congress, it is hard to conceive of taxpayers availing themselves of such a process if courts are subject to executive manipulation. Taxpayers will be rightly hesitant to undertake a lengthy and expensive challenge, even to the most unjust assessment, if the IRS is empowered to use its rulemaking authority to enact a belated defense to those claims.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

HOWARD R. RUBIN
Counsel of Record
ROBERT T. SMITH
KATTEN MUCHIN ROSENMAN LLP
2900 K Street, NW
North Tower – Suite 200
Washington, DC 20007
howard.rubin@kattenlaw.com
202-625-3500

Counsel for Amicus Curiae
Grapevine Imports, Ltd.

December 22, 2011

AMICUS CURIAE BRIEF

No. 11-139

In the Supreme Court of the United States

United States of America,
Petitioner,

v.

Home Concrete & Supply, LLC, et al.,
Respondents.

On Writ of Certiorari to
the United States Court of Appeals
for the Fourth Circuit

BRIEF OF *AMICUS CURIAE* PROFESSOR KRISTIN E. HICKMAN IN SUPPORT OF RESPONDENTS

Kristin E. Hickman
Amicus Curiae and Counsel of Record
University of Minnesota Law School
229 – 19th Avenue South
Minneapolis, MN 55455
(612) 624-2915
khickman@umn.edu

2011 – Bachman Legal Printing ■ (612) 339-9518 ■ 1-800-715-3582 ■ Fax (612) 337-8053

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES iii

INTEREST OF THE *AMICUS CURIAE* 1

SUMMARY OF THE ARGUMENT 3

ARGUMENT 6

I. TREAS. REG. § 301.6501(E)-1 IS PROCEDURALLY INVALID. 6

A. Treasury Failed To Comply With APA § 553 In Promulgating Treas. Reg. § 301.6501(e)-1..... 7

B. No Statutory Exception Excuses Treasury's Failure To Comply With APA § 553..... 13

1. IRC § 7805(e) Does Not Authorize Treasury To Disregard APA § 553..... 14

2. Treas. Reg. § 301.6501(e)-1 Is Not An Interpretative Rule.... 19

3. The Good Cause Exception Does Not Apply To Treas. Reg. § 301.6501(e)-1..... 24

C. Treasury's Post-Promulgation Notice And Comment In Finalizing Temp. Treas. Reg. § 301.6501(e)-1T Does Not Cure The Procedural Violation..... 26

II. THE COURT SHOULD NOT EXTEND *CHEVRON* DEFERENCE TO AGENCY REGULATIONS PROMULGATED IN VIOLATION OF CONGRESSIONALLY IMPOSED PROCEDURAL REQUIREMENTS.. 32

CONCLUSION..... 35

TABLE OF AUTHORITIES

Page(s)

Cases:

Advocates for Highway & Auto Safety v. Fed. Highway Admin., 28 F.3d 1288 (D.C. Cir. 1994)..... 27

Air Transp. Ass'n of Am. v. Dep't of Transp., 900 F.2d 369 (D.C. Cir. 1990), *vacated without opinion and remanded*, 498 U.S. 1023 (1991), *vacated as moot*, 933 F.2d 1043 (D.C. Cir. 1991)..... 26

American Hospital Ass'n v. Bowen, 834 F.2d 1037 (D.C. Cir. 1987)..... 6

American Mining Congress v. Mine Safety & Health Admin., 995 F.2d 1106 (D.C. Cir. 1993)..... 22

Asiana Airlines v. FAA, 134 F.3d 393 (D.C. Cir. 1998)..... 15, 17, 33

Bohner v. Daniels, 243 F. Supp. 2d 1171 (D. Or. 2003)..... 24

Burks v. United States, 633 F.3d 347 (5th Cir. 2011)..... 32

Buschmann v. Schweiker, 676 F.2d 352 (9th Cir. 1982)..... 24

Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 465 U.S. 837 (1984)..... *passim*

Chrysler Corp. v. Brown, 441 U.S. 281 (1979)..... 19

Colony v. Comm'r, 357 U.S. 28 (1958)..... 30

Comm'r v. Beard, 633 F.3d 616 (7th Cir. 2011)..... 32

Dickinson v. Zurko, 527 U.S. 150 (1999)..... 15

Estate of Gerson v. Comm'r, 507 F.3d 435 (6th Cir. 2007)..... 9

Judulang v. Holder, No. 10-694, 2011 WL 6141311 (U.S. Dec. 12, 2011)..... 34

Lake Carriers' Ass'n v. EPA, 652 F.3d 1 (D.C. Cir. 2011)..... 15

Levesque v. Block, 723 F.2d 175 (2d Cir. 1983)..... 11, 27, 29

Mayo Foundation for Medical Educ. and Research v. United States, 131 S.Ct. 704 (2011)..... *passim*

Morton v. Ruiz, 415 U.S. 199, 232, 236 (1974)..... 19

Motor Vehicle Mfrs. Ass'n of United States, Inc. v. State Farm Mut. Automobile Ins. Co., 463 U.S. 29 (1983)..... 34

National Ass'n of Regulatory Utility Comm'rs v. ICC, 41 F.3d 721 (D.C. Cir. 1994)..... 34

National Tour Brokers Ass'n v. United States, 591 F.2d 896 (D.C. Cir. 1978)..... 12

Natural Res. Def. Council, Inc. v. EPA, 683 F.2d 752 (3d Cir. 1982)..... 27

Radzanlower v. Touche Ross & Co., 426 U.S. 148 (1976)..... 15

SEC v. Chenery Corp., 318 U.S. 80 (1943)..... 10

Sharon Steel Corp. v. EPA, 597 F.2d 377 (3d Cir. 1979)..... 12, 27

Smiley v. Citibank (South Dakota), N.A., 517 U.S. 735 (1996)..... 33

U.S. Steel Corp. v. EPA, 605 F.2d 283 (7th Cir. 1979)..... 27

United States v. Mead Corp.,
533 U.S. 218 (2001)..... 1, 22, 33

Vimar Seguros Y Reaseguros, S.A. v. M/V Sky Reefer,
515 U.S. 528 (1995)..... 15

Statutes:

Administrative Procedure Act (5 U.S.C.)

§ 553..... *passim*

§ 553(b)..... 7, 13, 34

§ 553(b)(A)..... 4

§ 553(b)(B)..... 4

§ 553(c)..... *passim*

§ 559..... 15

§ 706..... 29

§ 706(2)(A) 34

§ 706(2)(D) 6-7, 34

Internal Revenue Code (26 U.S.C.)

§ 6501(e) 2, 3, 19, 31, 32

§ 6662(a)-(b)(1), (c) 9

§ 6694(b) 9

§ 7805(e) ..... *passim*

§ 7805(e)(1) 14

§ 7805(e)(2) 14

49 U.S.C. § 45301(b)(2)..... 17

Treasury Regulations and Other Regulatory Materials:

2009-43 I.R.B. 551..... 10

2011-6 I.R.B. 455..... 10

74 Fed. Reg. 49322 (Sept. 28, 2009)..... 25

74 Fed. Reg. 49,354 (Sept. 28, 2009)..... 10

T.D. 9466, 74 Fed. Reg. 49321 (Sept. 28, 2009), 2009-43 I.R.B. 551..... 9-10, 13, 25, 30

T.D. 9511, 75 Fed. Reg. 78897 (Dec. 17, 2010)..... 10, 13, 25

Temp. Treas. Reg. (26 C.F.R.) § 301.6501(e)-1T. *passim*

Treasury Regulations (26 C.F.R.)

§ 1.6662-3(b)(2)..... 9

§ 1.6694-3(e)..... 9

§ 31.3121(b)(10)-2(d)..... 23

§ 301.6501(e)-1..... *passim*

Miscellaneous:

Administrative Conference of the United States, *Notice; Adoption of Recommendations*, 60 Fed. Reg. 43108, 43111 (Aug. 18, 1995)..... 8, 11, 12, 14

Appellee's Petition for Panel Rehearing, *Salman Ranch, Ltd. v. United States*, 573 F.3d 1362 (Fed. Cir. 2009) (No. 2008-5053), 2009 WL 361165... 10

Bernard Schwartz, Administrative Law (3d ed. 1991)..... 6

Brief for the Appellant, *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 650 F.3d 691 (D.C. Cir. 2011) (No. 10-1204), 2010 WL 6210551..... 14

Brief for the Appellee, *United States v. Home Concrete & Supply, LLC*, (No. 09-2353) (4th Cir. Apr. 30, 2010)..... 13, 20

Charles H. Koch, Jr., Administrative Law and Practice (3d ed. 2010)..... 25

Irving Salem et al., *ABA Section of Taxation Report of the Task Force on Judicial Deference*, 57 Tax Law. 717 (2004)..... 9, 18, 20

Jeremiah Coder, *IRS Strikes Back Against Judicial Losses in Overstated Basis Cases*, 125 Tax Notes 19 (Oct. 5, 2009)..... 30, 31

Jeremiah Coder, *IRS Undeterred After Tax Court's Intermountain Decision*, 127 Tax Notes 729 (May 17, 2010)..... 31

Juan F. Vasquez, Jr. & Peter A. Lowy, *Challenging Temporary Treasury Regulations*, 3 Hous. Bus. & Tax L.J. 248 (2003)..... 18

Kenneth Culp Davis, Administrative Law Treatise (1958)..... 21

Kenneth Culp Davis, *Administrative Rules—Interpretative, Legislative, and Retroactive*, 57 Yale L.J. 919 (1948)..... 21

Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727 (2007)..... 2, 17, 26, 28

Kristin E. Hickman, *The Need for* Mead*: Rejecting Tax Exceptionalism In Judicial Deference*, 90 Minn. L. Rev. 1537 (2007)..... 22

Michael Asimow, *Interim-Final Rules: Making Haste Slowly*, 51 Admin. L. Rev. 703 (1999)..... 8, 11, 28

Michael Asimow, *Public Participation in the Adoption of Temporary Treasury Regulations*, 44 Tax Law. 343 (1991)..... 16, 17, 18

Reply Brief for the Appellant, *Wilmington Partners L.P. v. Comm'r*, (No. 10-4183) (2d Cir. May 19, 2011), 2011 WL 2113367..... 13

Respondent's Brief in Support of Motion to Vacate Order and Decision, *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 134 T.C. 211 (2010) (No. 25868-06), 2010 WL 2285587..... 10

Richard J. Pierce, Jr., Administrative Law Treatise (5th Ed. 2010)..... 19, 21, 23

Ronald M. Levin, *The Anatomy of* Chevron*: Step Two Reconsidered*, 72 Chi-Kent L. Rev. 1253 (1997)..... 34

Stanley S. Surrey, *The Scope and Effect of Treasury Regulations Under the Income, Estate, and Gift Taxes*, 88 U. Pa. L. Rev. 556 (1940)..... 21

Stephanie Stern, *Cognitive Consistency: Theory Maintenance and Administrative Rulemaking*, 63 U. Pitt. L. Rev. 589 (2002)..... 12

Thomas W. Merrill & Kathryn Tongue Watts, *Agency Rules with the Force of Law: The Original Convention*, 116 Harv. L. Rev. 467 (2002)..... 22

INTEREST OF *AMICUS CURIAE*[1]

Amicus is a Professor of Law at the University of Minnesota Law School who teaches and writes in the areas of tax and administrative law. *Amicus* has a longstanding academic interest in issues implicated by this case. *Amicus* has written extensively about judicial review of agency legal interpretations both generally and in the context of tax cases. *See, e.g.*, Kristin E. Hickman & Matthew D. Krueger, *In Search of the Modern* Skidmore *Standard*, 107 Colum. L. Rev. 1235 (2007); Kristin E. Hickman, *The Need for* Mead, *Rejecting Tax Exceptionalism in Judicial Deference*, 90 Minn. L. Rev. 1537 (2006); Thomas W. Merrill & Kristin E. Hickman, Chevron's *Domain*, 89 Geo. L.J. 833 (2001). This Court has previously cited *Amicus*'s work regarding the scope of *Chevron* review. *See United States v. Mead Corp.*, 533 U.S. 218, 230 n.11 (2001). *Amicus* has also written extensively about the interplay between the Administrative Procedure Act (APA) and the Internal Revenue Code (IRC) as well as the comparability of APA procedural requirements with Treasury Department and Internal Revenue Service practices in administering the IRC. *See, e.g.*, Kristin E. Hickman, *IRB Guidance: The No Man's Land of Tax Code Interpretation*, 2009 Mich. St. L. Rev. 239;

---

[1] Consistent with Supreme Court Rule 37.3(a), *Amicus* files this brief with the written consent of both parties. Consistent with Supreme Court Rule 37.6, *Amicus* hereby certifies that this brief was not authored in whole or in part by counsel for any party and that *Amicus* received no monetary contribution toward the preparation or submission of this brief other than the general financial support of the academic institution with which she is affiliated.

Kristin E. Hickman, *A Problem of Remedy: Responding to Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 76 Geo. Wash. L. Rev. 1154 (2008); and, Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727 (2007). *Amicus* also co-authors an administrative law textbook, *see* Kristin E. Hickman & Richard J. Pierce, Jr., Federal Administrative Law (2010).

This case raises significant issues of administrative law and tax administration that reach far beyond Treas. Reg. § 301.6501(e)-1 and the parties at bar. Consistent with her scholarly interests, *Amicus* submits this brief solely to address issues regarding the procedures utilized by the Treasury Department in promulgating Treas. Reg. § 301.6501(e)-1 and the resulting implications for the standard of review for evaluating Treas. Reg. § 301.6501(e)-1. *Amicus* disclaims any view regarding either the clarity of Internal Revenue Code § 6501(e) or the substantive reasonableness of Treas. Reg. § 301.6501(e)-1 as an interpretation of that statute. *Amicus* hopes this brief will assist the Court in resolving the important questions of administrative law and tax administration raised by this case.

INTRODUCTION AND SUMMARY OF THE ARGUMENT

To the government, this is a case about a tax shelter, the Son-of-BOSS transaction, and about whether the Court will respect Treasury's interpretation of the six year limitations period of Internal Revenue Code (IRC) § 6501(e), 26 U.S.C. § 6501(e), to allow the government to continue its pursuit of taxpayers who participated in Son-of-BOSS transactions to the detriment of the fisc. (Gov't Br. at 2-10.) Of course, Treasury's position affects many more taxpayers engaged in run-of-the-mill asset sales than merely participants in Son-of-BOSS transactions. Most significantly however, this is a case about the power of federal government agencies to define the parameters of the laws that they administer, the limitations that Congress has imposed on agencies as they exercise that power, and the role of the courts in policing agency action.

In the event this Court decides that IRC § 6501(e) is ambiguous, the government claims that Treas. Reg. § 301.6501(e)-1 resolves the case and is entitled to *Chevron* deference. (Gov't Br. at 12, 37-39.) Throughout the litigation giving rise to this case, the procedural validity of Treas. Reg. § 301.6501(e)-1 and its temporary predecessor, Temp. Treas. Reg. § 301.6501(e)-1T, and the significance of those regulations' procedural invalidity for judicial review under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 465 U.S. 837 (1984), have been the subject of disagreement among the litigants and the lower courts. Assessing whether the Court should extend *Chevron* deference to Treas. Reg. §

301.6501(e)-1 potentially raises several previously unaddressed questions of administrative law doctrine generally and tax administration particularly.

First, did the procedures by which the Treasury Department (Treasury) adopted Treas. Reg. § 301.6501(e)-1 and its predecessor, Temp. Treas. Reg. § 301.6501(e)-1, violate or comply with congressionally imposed procedural requirements? In adopting these regulations, Treasury employed an inverted procedural sequence known commonly in administrative law as interim-final rulemaking—issuing legally binding, temporary regulations with only post-promulgation notice and comment undertaken in the course of replacing the temporary regulations with final ones. In the absence of a valid claim to an exception from pre-promulgation notice and comment under APA § 553, courts and scholars have sharply criticized interim-final rulemaking as noncompliant with either the letter or the spirit of the Administrative Procedure Act (APA). Neither the language of IRC § 7805(e) nor the interpretative rule exception of APA § 553(b)(A) excuses Treasury's deviation from APA procedural requirements, and Treasury has simply failed to articulate a good cause claim under APA § 553(b)(B) in connection with Treas. Reg. § 301.6501(e)-1 or its temporary predecessor. The lower courts have struggled, however, to find an appropriate remedy when agencies engage in procedurally improper interim-final rulemaking. While invalidating a regulation adopted invalidly through interim-final rulemaking may not always the best remedy, the Court should grant that remedy in this case and invalidate Treas. Reg. § 301.6501(e)-1. The fact that Treasury failed to

comply with APA procedural requirements in the course of promulgating Treas. Reg. § 301.6501(e)-1 for the purpose of influencing ongoing litigation, taken together, should disqualify that regulation from judicial leniency.

A second question raised by this case concerns the relationship between procedural compliance and *Chevron* deference. Even if the Court is inclined to conclude that Treas. Reg. § 301.6501(e)-1 reflects a *substantively* permissible interpretation of IRC § 6501(e), it does not necessarily follow that *Chevron* deference is appropriate for a regulation that fails to satisfy congressionally-imposed *procedural* requirements. Although the Court has declined to deny *Chevron* deference as a general rule either to regulations lacking notice and comment or adopted in the course of litigation, the Court has also linked the *Chevron* step two inquiry with broader compliance with the APA. In this case, Treasury's lack of compliance with APA § 553 should lead the Court to declare Treas. Reg. § 301.6501(e)-1 unreasonable at *Chevron* step two.

ARGUMENT

I. TREAS. REG. § 301.6501(E)-1 IS PROCEDURALLY INVALID.

Modern American government consists of a conglomeration of executive and independent agencies with thousands of officials exercising tremendous delegated power not only to execute the laws as enacted by Congress but indeed to define in great detail what those laws are. When agencies exercise delegated power to adopt regulations carrying the force and effect of law, they generally are bound to follow certain procedures mandated by Congress to ensure transparency and accountability and to gain democratic legitimacy through public participation. *See* Bernard Schwartz, Administrative Law § 4.12 (3d ed. 1991). Consistent with these goals, absent express congressional command to the contrary, APA § 553 provides the procedures that govern agency rulemaking. *See* 5 U.S.C. § 553. Much like the legislative process, APA § 553 prescribes a regime of public notice and comment in the promulgation of agency rules, thus "reintroduce[ing] public participation and fairness to affected parties after governmental authority has been delegated to unrepresentative agencies." *American Hospital Ass'n v. Bowen*, 834 F.2d 1037, 1044 (D.C. Cir. 1987) (quoting *Batterton v. Marshall*, 648 F.2d 694, 703 (D.C. Cir. 1980)). Agency regulations are legally invalid if they fail to comply with the procedural requirements of APA § 553 or else to qualify for a specific exception therefrom. *See* 5 U.S.C. § 706(2)(D) (instructing reviewing courts to invalidate agency

actions found to be "without observance of procedure required by law").

A. Treasury Failed To Comply With APA § 553 In Promulgating Treas. Reg. § 301.6501(e)-1.

To advance the goals of transparency, accountability, public participation and fairness in agency rulemaking, APA § 553 contemplates a particular procedural sequence for agencies adopting regulations that carry the force and effect of law. APA § 553(b) requires an agency to provide public notice of its proposed rulemaking through publication in the Federal Register. *See* 5 U.S.C. § 553(b). Next, APA § 553(c) commands the agency pursuing the rulemaking process to offer interested persons an opportunity to participate through the submission of written comments. *See* 5 U.S.C. § 553(c) (calling for opportunity to comment "after notice"). Only "after consideration of the relevant matter presented" through the comments may the agency issue final regulations along with a "concise general statement of their basis and purpose." *Id.* In other words, the APA anticipates that regulated parties will receive notice of proposed agency rules and have the opportunity to submit comments *before* finding themselves legally bound by those rules.

Though establishing notice-and-comment rulemaking as the default, Congress acknowledged that not all agency rules necessitate such extensive procedures. Thus, APA § 553 provides exceptions for interpretative rules, procedural rules, and policy statements. *See* 5 U.S.C. § 553(b)(A). Additionally,

Congress recognized that, in some instances, agencies may legitimately need to issue legally binding rules without public notice and comment. Hence, APA § 553 authorizes agencies to dispense with notice and comment "when the agency for good cause finds (and incorporates the finding and a brief statement of reasons therefore in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest." 5 U.S.C. § 553(b)(B).

Treasury did not follow the procedural sequence contemplated by APA § 553 in promulgating Treas. Reg. § 301.6501(e)-1. Instead, though without using the label, Treasury employed an alternative procedural sequence known most commonly by courts and administrative law scholars as "interim-final rulemaking." Specifically, interim-final rulemaking occurs when an agency issues legally-binding rules without notice and comment but simultaneously requests post-promulgation public comment with the promise that the agency will consider comments received and may make modifications in adopting replacement final rules. *See, e.g.*, Michael Asimow, *Interim-Final Rules: Making Haste Slowly*, 51 Admin. L. Rev. 703, 704 (1999) (describing interim-final rulemaking); Administrative Conference of the United States, *Notice; Adoption of Recommendations*, 60 Fed. Reg. 43108, 43111 (Aug. 18, 1995) (same). In other words, with interim-final rulemaking, the agency begins with the legal equivalent of a final rule rather than with merely a nonbinding proposal, thus inverting the procedural sequence contemplated by APA § 553 and tainting the procedural validity of the

replacement rules adopted after post-promulgation notice and comment.

Consistent with the interim-final rulemaking pattern, here Treasury began its rulemaking process in September 2009 by issuing and publishing in the Federal Register and the Internal Revenue Bulletin a "temporary" but legally binding regulation, Temp. Treas. Reg. § 301.6501(e)-1T, without pre-promulgation notice and comment.[2] *See* T.D. 9466,

---

[2] Lest there be any doubt regarding its status for both taxpayers and the government, Temp. Treas. Reg. § 301.6501(e)-1 carried precisely the same legal force as the final Treas. Reg. § 301.6501(e)-1. As a general matter, temporary as well as final Treasury regulations are legal equivalents. Both temporary and final Treasury regulations are published in the Code of Federal Regulations. In interpreting congressionally-enacted penalty provisions requiring taxpayers and tax return preparers to comply with tax "rules or regulations," 26 U.S.C. § 6662(a)-(b)(1), (c); 26 U.S.C. § 6694(b), Treasury through regulations has defined rules or regulations to include all "temporary or final Treasury regulations issued under the [IRC]." Treas. Reg. §§ 1.6662-3(b)(2), 1.6694-3(e). As a result, Treasury, the Internal Revenue Service, tax professionals, taxpayers, and the courts all operate with the understanding that temporary and final Treasury regulations are equally binding on taxpayers and the government. *See, e.g.*, *Estate of Gerson v. Comm'r*, 507 F.3d 435, 438 (6th Cir. 2007) (noting that both temporary and final Treasury regulations are legally binding); Irving Salem et al., *ABA Section of Taxation Report of the Task Force on Judicial Deference*, 57 Tax Law. 717, 735 (2004) ("Unlike proposed regulations, temporary regulations are effective when they initially appear in the Federal Register, thus providing immediate and binding guidance to taxpayers."). Though Temp. Treas. Reg. § 301.6501(e)-1T concerned the limitations period for assessing a tax deficiency and thus was not the sort of regulation to give rise to penalty potential directly, the government quite clearly signaled Treasury's intent regarding the temporary regulation's legal force through various court

74 Fed. Reg. 49321 (Sept. 28, 2009), 2009-43 I.R.B. 551. Simultaneously, Treasury issued and published in the Federal Register a notice of proposed rulemaking advancing precisely the same regulatory language as the temporary regulation and inviting public comment. *See* 74 Fed. Reg. 49,354 (Sept. 28, 2009). Subsequently, in December 2010, after contemplating the comment that it received, Treasury withdrew the temporary regulation and published the final regulation at issue in this case. *See* T.D. 9511, 75 Fed. Reg. 78897 (Dec. 17, 2010), 2011-6 I.R.B. 455. As the government acknowledges, "[t]he text of the final regulation tracks the temporary regulation in virtually every respect." (Gov't Br. 28-29.)

Notice-and-comment rulemaking is time consuming, and particularly where the good cause exception applies, agencies may feel the need to act more quickly but still value public input. Accordingly, practitioners and scholars have applauded interim-final rulemaking as an important

---

documents filed shortly thereafter. *See, e.g.*, Respondent's Brief in Support of Motion to Vacate Order and Decision at n.2, *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 134 T.C. 211 (2010) (No. 25868-06), 2010 WL 2285587 (analogizing the issuance of Temp. Treas. Reg. § 301.6501(e)-1T to the extension by a legislature of a statute of limitations during an appeal of a court ruling, thus requiring the court to apply the new limitations period); Appellee's Petition for Panel Rehearing, *Salman Ranch, Ltd. v. United States*, 573 F.3d 1362 (Fed. Cir. 2009) (No. 2008-5053, 2009 WL 361165 at *1-2, 8-9, 13-14 (describing Temp. Treas. Reg. § 301.6501(e)-1T as an "intervening legal development[ ]" requiring the court to reconsider its opinion, as entitled to *Chevron* deference, and as compelling an outcome in favor of the government).

compromise between agency flexibility and efficiency on the one hand and the legitimacy gained through public participation in the rulemaking process on the other, *but only when the rules in question qualify for an exception from the procedural requirements of APA § 553.* Otherwise, the legal consensus holds that interim-final rulemaking violates the APA. *See, e.g.*, Administrative Conference of the United States, *supra*, at 43111-12 ("Courts generally have not allowed post-promulgation comment as an alternative to the prepromulgation notice-and-comment process in situations where no exemption is justified."); Asimow, *Interim-Final Rules*, *supra*, at 717, 725-26 (observing that, "absent such an exception, a rule adopted with post- rather than pre-adoption notice and comment is procedurally invalid," but criticizing that conclusion).

The reasons for this conclusion are two-fold. First, as noted above, because interim-final rulemaking begins the rulemaking process with the legal equivalent of a final rule, without a valid exception, the procedural sequence deviates from the congressionally-enacted text of APA § 553. Second, courts and scholars have long recognized that inverting the APA procedural sequence by beginning with legally-binding temporary or interim-final rules conveys a stronger message of agency commitment to a particular outcome, chills public participation, and thus undermines the very congressional goals that notice-and-comment rulemaking is designed to advance. *See, e.g.*, *Levesque v. Block*, 723 F.2d 175, 187-88 (1st Cir. 1983) ("[C]itizens will recognize that the agency is less likely to pay attention to their views after a rule is in place, and therefore the public

is less likely to participate vigorously in comment."); *Sharon Steel Corp. v. EPA*, 597 F.2d 377, 381 (3d Cir. 1979) (reflecting similar concern); Administrative Conference of the United States, *supra*, at 43112 (discouraging agency use of interim-final rulemaking on such grounds); *cf. National Tour Brokers Ass'n v. United States*, 591 F.2d 896, 902 (D.C. Cir. 1978) ("People naturally tend to be more close-minded and defensive once they have made a 'final' determination."); Stephanie Stern, *Cognitive Consistency: Theory Maintenance and Administrative Rulemaking*, 63 U. Pitt. L. Rev. 589, 620-30 (2002) (drawing from academic literature in cognitive psychology to support a similar thesis regarding even standard notices of proposed rulemaking that offer draft regulatory language).

In its opening brief, the government contended that, because Treasury adopted the final Treas. Reg. § 301.6501(e)-1 after public notice and comment, a procedural challenge against Temp. Treas. Reg. § 301.6501(e)-1T was rendered "irrelevant to the proper disposition of this case." (Gov't Br. at 29.) This claim misses the point. To be absolutely clear, the procedural flaw is not merely with Temp. Treas. Reg. § 301.6501(e)-1T for its lack of pre-promulgation notice and comment. Rather, final Treas. Reg. § 301.6501(e)-1 is also invalid because Treasury started its rulemaking for that regulation with a legally-binding temporary regulation rather solely with a notice of proposed rulemaking, thus inverting the procedural sequence outlined in APA § 553.

B. No Statutory Exception Excuses Treasury's Failure To Comply With APA § 553.

As noted above, APA § 553 includes several exceptions from notice-and-comment rulemaking—for interpretative rules, procedural rules, policy statements, and good cause. Congress, of course, can and sometimes does provide specific exceptions from APA § 553 in other statutes.

In the preambles to both Temp. Treas. Reg. § 301.6501(e)-1T and Treas. Reg. § 301.6501(e)-1T, Treasury offered no justification for dispensing with pre-promulgation notice and comment beyond the bald assertion that APA § 553(b) "does not apply to these regulations." T.D. 9511, 75 Fed. Reg. 78897, 78898 (Dec. 17, 2010); T.D. 9466, 74 Fed. Reg. 49321, 49322 (Sept. 28, 2009). In its opening brief, the government cursorily made a claim that it has developed more fully before the circuit courts, that IRC § 7805(e) authorizes its departure from APA § 553. (Gov't Br. at 29.) Though not in its opening brief before this Court, throughout this litigation and in other cases challenging Treas. Reg. § 301.6501(e)-1, the government has contended that both Treas. Reg. § 301.6501(e)-1 and its temporary predecessor are exempt from APA procedural requirements as interpretative rules. *See* Brief for the Appellee at 39-42, *United States v. Home Concrete & Supply, LLC*, (No. 09-2353) (4th Cir. Apr. 30, 2010); *see also, e.g.*, Reply Brief for the Appellant, *Wilmington Partners L.P. v. Comm'r*, (No. 10-4183) (2d Cir. May 19, 2011), 2011 WL 2113367 at *25-26 (claiming that Treas. Reg. § 301.6501(e)-1 is an interpretative rule); Brief

for the Appellant at 52-60, *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 650 F.3d 691 (D.C. Cir. 2011) (No. 10-1204), 2010 WL 6210551 (arguing that Temp. Treas. Reg. § 301.6501(e)-1 is an interpretative rule). Finally, agencies using interim-final rulemaking usually claim the good cause exception. *See* Administrative Conference of the United States, *supra*, at 43111. None of these alternatives operate to excuse Treasury's lapse in this case.

1. IRC § 7805(e) Does Not Authorize Treasury To Disregard APA § 553.

IRC § 7805(e) does two things. First, when Treasury issues a temporary regulation, IRC § 7805(e)(1) requires Treasury to issue a corresponding notice of proposed rulemaking. *See* 26 U.S.C. § 7805(e)(1) ("Any temporary regulation issued by the Secretary shall also be issued as a proposed regulation."). Second, IRC § 7805(e)(2) sunsets temporary regulations after three years, thus setting a time frame within which Treasury must complete APA notice-and-comment procedures to finalize any temporary regulation it issues and wishes to retain. *See* 26 U.S.C. § 7805(e)(2) ("Any temporary regulation shall expire within 3 years after the date of issuance of such regulation."). The government's reliance on this language to excuse its failure to comply with APA rulemaking requirements is misplaced and should be rejected by this Court.

Congress certainly has the power to alter APA procedural requirements in specific instances. However, Congress has also instructed the courts

that "[s]ubsequent statute may not be held to supersede or modify" APA rulemaking requirements "except to the extent that it does so expressly." 5 U.S.C. § 559. Consistent with this provision, this Court has adopted a policy of uniformity in administrative law absent clear congressional command to the contrary. *See, e.g., Mayo Foundation for Medical Educ. and Research v. United States*, 131 S.Ct. 704, 713 (2011) (expressing disinclination for carving out a tax law exception from general administrative law principles); *Dickinson v. Zurko*, 527 U.S. 150, 155 (1999) ("The APA was meant to bring uniformity to a field full of variation and diversity. It would frustrate that purpose to permit divergence on the basis of a requirement 'recognized' only as ambiguous."). Hence, while by no means binding this Court, the lower courts have generally "looked askance at agencies' attempts to avoid the standard notice and comment procedures" and have construed supposed statutory exceptions from APA § 553 narrowly. *Lake Carriers' Ass'n v. EPA*, 652 F.3d 1, 6 (D.C. Cir. 2011) (quoting *Asiana Airlines v. FAA*, 134 F.3d 393, 396 (D.C. Cir. 1998), and *New Jersey v. EPA*, 626 F.2d 1038, 1045 (D.C. Cir. 1980)). Finally, absent clearly expressed congressional intent to the contrary, this Court has consistently advised construing seemingly competing statutes harmoniously to give effect to all. *See, e.g., Vimar Seguros Y Reaseguros, S.A. v. M/V Sky Reefer*, 515 U.S. 528, 533 (1995); *Radzanlower v. Touche Ross & Co.*, 426 U.S. 148, 154-55 (1976).

IRC § 7805(e) fails to satisfy the high threshold for recognition as an exception from APA rulemaking requirements, as its terms are easily reconciled with

APA § 553. Further, a more cooperative reading of the two provisions better fits the history surrounding the enactment of IRC § 7805(e).

Contrary to the government's claim, the text of IRC § 7805(e) authorizes nothing. Rather, the text of IRC § 7805(e) is better read as restricting Treasury's authority by imposing limitations on Treasury: *if* Treasury issues temporary regulations, *then* Treasury must simultaneously issue a notice of proposed rulemaking and finalize its temporary regulations within three years. As already discussed in Part I.A. above, as with other agencies, APA § 553 authorizes Treasury to adopt legally binding temporary regulations without notice and comment *so long as Treasury falls within the good cause exception offered by APA § 553(b).* Under APA § 553, however, an agency that issues temporary or interim final regulations pursuant to a good cause claim is under no fixed obligation to pursue post-promulgation notice and comment. Thus, acknowledging that Treasury, like other agencies, has the power to and sometimes does adopt temporary regulations without public notice and comment, and operating under the assumption that Treasury has done validly so within the parameters established by APA § 553, IRC § 7805(e) imposes extra requirements on Treasury to publish a notice of proposed rulemaking immediately and act upon submitted comments within three years. *See* Michael Asimow, *Public Participation in the Adoption of Temporary Treasury Regulations*, 44 Tax Law. 343, 363 (1991) (advocating this reading of IRC § 7805(e)).

This cooperative reading of APA § 553 and IRC § 7805(e) stands in stark contrast to the more obvious irreconcilability of other congressional commands with APA § 553. For example, in the Federal Aviation Reauthorization Act, Congress instructed the Federal Aviation Authority to "publish in the Federal Register an initial fee schedule and associated collection process as an interim final rule, pursuant to which public comment will be sought and a final rule issued." 49 U.S.C. § 45301(b)(2). In upholding the agency's issuance of an interim final rule without notice and comment or a good cause claim, the reviewing court observed that requiring notice and comment both before and after the FAA published its interim final rule would render the post-issuance notice and comment largely superfluous. *See Asiana Airlines v. FAA*, 134 F.3d 393, 398 (D.C. Cir. 1998). This example is easily distinguishable from the relationship between APA § 553 and IRC § 7805(e) since, as demonstrated in the preceding paragraph, those provisions can be read cooperatively in a way that eliminates any redundancy.

Furthermore, reading APA § 553 and IRC § 7805(e) cooperatively in this manner better effectuates the congressional purpose driving that provision's adoption. Congress adopted IRC § 7805(e) in 1988 as part of the Taxpayer Bill of Rights. Treasury had only started issuing temporary regulations without pre-promulgation notice and comment regularly in the 1980s. *See* Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 Notre

Dame L. Rev. 1727, 1797 (2007), (describing the evolution of Treasury's use of temporary regulations); Asimow, *Public Participation*, *supra*, at 343 (linking temporary Treasury regulations to the 1980s). Then, as now, Treasury maintained that most of its regulations were exempt from APA § 553 requirements as interpretative rules. But up until the 1980s, Treasury had routinely followed APA § 553 procedures regardless in adopting its regulations. As documented extensively by Professor Michael Asimow, Congress's primary concern in adopting IRC § 7805(e) was the number of temporary Treasury regulations languishing on the books for several years with no indication of when or whether Treasury might finalize them using public notice and comment. *See* Asimow, *Public Participation*, *supra*, at 363-64; *see also* Irving Salem et al., *ABA Section of Taxation Report of the Task Force on Judicial Deference*, 57 Tax Law. 717, 735 (2004) (recognizing same); Juan F. Vasquez, Jr. & Peter A. Lowy, *Challenging Temporary Treasury Regulations*, 3 Hous. Bus. & Tax L.J. 248, 254 (2003) (describing similar reasons for adopting IRC § 7805(e)). Wanting Treasury to stop avoiding notice and comment, and accepting without further inquiry Treasury's position that most of its regulations were exempt from APA notice and comment requirements as interpretative rules, Congress contemplated language eliminating or restricting the interpretative rule exception in the tax context. *See id.* Ultimately instead, Congress chose to require post-promulgation notice and comment within three years. *See id.* In short, Congress adopted the requirements of IRC § 7805(e) as additions to rather than subtractions from the requirements of APA § 553, and with the goal of more

rather than less public participation in the development of Treasury regulations.

2. Treas. Reg. § 301.6501(e)-1 Is Not An Interpretative Rule.

The APA does not define the interpretative rule category, and the Court has had little occasion to do so precisely, either. Nevertheless, the Court has observed that legislative rules are "binding" or carry the "force and effect of law," with the characteristic that they "affect[ ] individual rights and obligations," while interpretative rules lack these qualities. *Chrysler Corp. v. Brown*, 441 U.S. 281, 301-02 (1979) (quoting *Morton v. Ruiz*, 415 U.S. 199, 232, 236 (1974)). Hence, established administrative law doctrine holds that legislative rules carry the force of law, binding members of the public, the government, and even the courts to the extent such rules represent a legitimate exercise of agency authority. *See, e.g.*, 1 Richard J. Pierce, Jr., Administrative Law Treatise § 6.4 (5th ed. 2010). Interpretative rules, by contrast, bind no one. *See id.* While the precise parameters of the force of law concept are unclear, for the reasons discussed in footnote 2 of Part I.A. of this brief, both Treas. Reg. § 301.6501(e)-1 and Temp. Treas. Reg. § 301.6501(e)-1 plainly carry such legal force: all Treasury regulations are published in the Code of Federal Regulations and carry penalty potential; members of the tax community, including Treasury, consider all Treasury regulations to be legally binding on taxpayers and the government alike; and the government has repeatedly argued not just that the courts ought to be persuaded to adopt the government's interpretation of IRC § 6501(e) as

articulated in its regulations, but that those regulations are binding on the courts as well as taxpayers, controlling the outcome of this case and others.

In characterizing Treas. Reg. § 301.6501(e)-1 and its temporary predecessor as interpretative, the government has relied principally on two alternative arguments. First, the government has argued that, in adopting the regulations, Treasury relied on its general authority under IRC § 7805(a) to "prescribe all needful rules and regulations for the enforcement of" the IRC. *See, e.g.*, Brief for the Appellee at 41-42, *United States v. Home Concrete & Supply, LLC*, (No. 09-2353) (4th Cir. Apr. 30, 2010). Second, the government has claimed that the regulations merely elaborated an undefined and ambiguous statutory term and thus clarified rather than changed existing law. *See id.* at 39-40. These arguments reflect a fundamental misunderstanding of the scope of the interpretative rule exception.

The government's first argument derives from the tax community's historic habit of reserving the legislative rule label for specific authority Treasury regulations while referring to regulations adopted by exercising general authority under IRC § 7805(a) as "interpretative" or "interpretive." *See, e.g.*, Salem et al., *supra*, at 728. Both drawing from and contributing to this practice, Treasury claimed for decades that the vast majority of its regulations interpreting the Internal Revenue Code are promulgated under the general authority of IRC § 7805(a) and, thus, are interpretative rules exempt from notice-and-comment rulemaking under APA §

553. In fact, through at least the 1950s, the general consensus among courts and scholars held that a general authority grant (whether tax or nontax) that authorized legally binding regulations would violate the nondelegation doctrine under the United States Constitution and thus be constitutionally invalid. *See, e.g.*, Kenneth Culp Davis, *Administrative Rules—Interpretative, Legislative, and Retroactive*, 57 Yale L.J. 919, 928-29 (1948); Stanley S. Surrey, *The Scope and Effect of Treasury Regulations Under the Income, Estate, and Gift Taxes*, 88 U. Pa. L. Rev. 556, 557-58 (1940). Thus, for a long time, most Treasury regulations were indeed considered nonbinding—*i.e.*, lacking the force of law. *See* 1 Kenneth Culp Davis, Administrative Law Treatise § 5.03, at 300 (1958).

Understandings regarding the legal status of general authority regulations began to shift around the 1970s. Professor Richard Pierce has documented a dramatic rise in agency rulemaking in the late 1960s, traceable to (1) the enactment of several new federal statutes in the mid to late 1960s that gave new or existing agencies general rulemaking authority and (2) decisions of this Court that largely replaced formal rulemaking under APA §§ 556 and 557 with informal rulemaking under APA § 553 as the rulemaking norm and precluded judges from imposing procedural requirements beyond those expressed in APA § 553 upon informal rulemaking efforts. *See* 1 Richard J. Pierce, Jr., Administrative Law Treatise § 1.6 (5th Ed. 2010). Professors Thomas Merrill and Kathryn Watts have traced changing perceptions regarding the legal force of general authority regulations to efforts during that same period by agencies like the Federal Trade

Commission, the Food and Drug Administration, and the National Labor Relations Board to claim previously unasserted legislative authority under general authority grants. *See* Thomas W. Merrill & Kathryn Tongue Watts, *Agency Rules with the Force of Law: The Original Convention*, 116 Harv. L. Rev. 467, 549-70 (2002).[3]

In *Mayo Foundation for Medical Education and Research v. United States*, 131 S.Ct. 704 (2011), this Court acknowledged the demise of the specific versus general authority distinction in administrative law for purposes of assessing whether agency action carries the force of law and recognized that, when the Treasury Department promulgates general authority regulations like Treas. Reg. § 301.6501(e)-1, it seeks to bind regulated parties with legal force. *See id.* at 714. *Mayo* concerned the eligibility of general authority Treasury regulation for *Chevron* deference rather than its characterization as a legislative rule, but it is difficult to imagine that a general authority Treasury regulation could carry the force of law for one purpose and not the other.[4] Perhaps in light of

---

[3] Merrill and Watts suggest a different outcome with respect to general authority Treasury regulations, but do so based on a misconstruction of the penalty provisions in the War Revenue Act of 1917. *See* Kristin E. Hickman, *The Need for* Mead*: Rejecting Tax Exceptionalism In Judicial Deference*, 90 Minn. L. Rev. 1537, 1603-04 (2007) (addressing Merrill and Watts).

[4] In fact, courts and scholars have on occasion used language quite similar to the two-part inquiry for *Chevron* eligibility articulated in *United States v. Mead Corp.*, 533 U.S. 218 (2001), to describe the force of law distinction between legislative and interpretative rules. For example, in *American Mining Congress v. Mine Safety & Health Admin.*, the court described a legislative rule as arising "if Congress has delegated legislative

Mayo, the Internal Revenue Service recently amended the Internal Revenue Manual to concede that some general authority Treasury regulations might be legislative rules, even while it continues insist that "most IRS/Treasury regulations will be interpretative." Internal Revenue Serv., Internal Revenue Manual § 32.1.1.2.8 (reflecting changes dated Sept. 23, 2011, and providing that "[w]hether a regulation is promulgated under a specific grant of authority in the [IRC] does not govern whether the regulation is interpretative or legislative"). Hence, the government may well have decided to drop this argument altogether.

The government's second claim, that its regulations merely elaborated an undefined and ambiguous statutory term and thus clarified rather than changed the law, is really beside the point. Whether an agency rule merely elaborates undefined or ambiguous statutory terms may serve as an indicator that a rule is interpretative rather than legislative. Some such rules are interpretative. Others, however, are legislative. If an agency with the congressionally delegated power to bind regulated parties with the force and effect of law exercises that power to elaborate a previously undefined statutory term, then that rule carries the force of law and is legislative. *See* Pierce, *supra*, at § 6.4 ("A rule that performs an interpretative function is a legislative rule rather than an interpretative rule if the agency has the statutory authority to promulgate a legislative rule and the agency exercises that power.")

---

power to the agency and if the agency intended to exercise that power in promulgating the rule." *See* 995 F.2d 1106 (D.C. Cir. 1993).

Hence, the regulation at issue in *Mayo*, Treas. Reg. 31.3121(b)(10)-2(d), merely elaborated the meaning of the word "student" as utilized in the statute, yet this Court had no difficulty concluding that Treasury regulation was an exercise of delegated power and carried the force of law. *See* 131 S.Ct. at 714. Treas. Reg. § 301.6501(e)-1 is no different in this regard than the one in *Mayo*, except that the latter was promulgated consistently with the procedural requirements of APA § 553.

3. The Good Cause Exception Does Not Apply To Treas. Reg. § 301.6501(e)-1.

As noted, the usual justification that agencies offer for using interim-final rulemaking with post-promulgation notice and comment is the good cause exception of APA § 553(b)(B). That provision excuses agencies from engaging in pre-promulgation notice and comment "when the agency for good cause finds (and incorporates the finding and a brief statement of reasons therefor in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest." 5 U.S.C. § 553(b)(B). The government's failure to articulate a good cause claim in issuing either Temp. Treas. Reg. § 301.6501(e)-1 or Treas. Reg. § 301.6501(e)-1 should preclude its ability to rely on this exception now.

Ccourts generally require agencies asserting the good cause exception to do so expressly and contemporaneously. *See, e.g.*, *Buschmann v. Schweiker*, 676 F.2d 352, 356-57 (9th Cir. 1982);

Bohner v. Daniels, 243 F. Supp. 2d 1171, 1176 (D. Or. 2003); *see also* 1 Charles H. Koch, Jr., Administrative Law and Practice § 4.13[1] (3d ed. 2010) ("An agency cannot claim the 'good cause' exemption for the first time after its procedures have been challenged in court. It must invoke the exemption at the time of rulemaking and explain why it needs to bypass APA procedures."). The terms of APA § 553(b)(B) requires an agency claiming the exception to include both its finding of good cause and its reasons for that finding "in the rules issued." 5 U.S.C. § 553(b)(B). Reading this language strictly is consistent with the bedrock principal of administrative law, that reviewing courts should limit their evaluation of agency action to justifications offered contemporaneously. *See, e.g.*, *SEC v. Chenery Corp.*, 318 U.S. 80, 87-88 (1943) ("The grounds upon which an administrative order must be judged are those upon which the record discloses that its action was based."). Treasury did not mention the good cause exception by name or offer any particular reasons for avoiding notice and comment in the preambles to either Temp. Treas. Reg. § 301.6501(e)-1 or Treas. Reg. § 301.6501(e)-1. *See* T.D. 9511, 75 Fed. Reg. 78897, 78898 (Dec. 17, 2010); T.D. 9466, 74 Fed. Reg. 49321, 49322 (Sept. 28, 2009). To date, the government has not claimed the good cause exception as justifying its use of interim-final rulemaking for Treas. Reg. § 301.6501(e)-1 or offered any explanation, either contemporaneously or on a post hoc basis, for why pre-promulgation notice and comment were impracticable, unnecessary, or contrary to the public interest.

Moreover, Treasury's failure to mention the good cause exception in the preamble to its

regulations is prima facie evidence of its contemporaneous intent not to make such a claim. The Internal Revenue Manual, which guides Internal Revenue Service employees in drafting Treasury regulations, provides instructions for claiming good cause including proposed justifications and language to be included in the regulatory preamble, none of which were included here.[5] *See* Internal Revenue Serv., Internal Revenue Manual § 32.1.5.4.7.5.1. The government should not be able to maintain claim to the good cause exception at this late date, in a reply brief before this Court.

C. Treasury's Post-Promulgation Notice And Comment In Finalizing Temp. Treas. Reg. § 301.6501(e)-1T Does Not Cure The Procedural Violation.

While courts and scholars agree that temporary or interim-final rules such as those used by Treasury in adopting Treas. Reg. § 301.6501(e)-1 violate APA § 553(b), they disagree over how to handle the breach. Courts have sometimes simply invalidated the succeeding final regulations. *See,*

---

[5] For many years, the Internal Revenue Manual merely instructed IRS employees to include the following language in regulatory preambles to claim good cause: "These regulations are necessary to provide taxpayers with immediate guidance." *See* Hickman, *Coloring Outside the Lines*, *supra*, at 1781 (documenting manual's language at that time and identifying several Treasury Decisions containing such language). Earlier this year, on September 30, 2011, the Internal Revenue Service updated the Internal Revenue Manual retaining this instruction but identifying additional considerations potentially supporting a good cause claim. *See* Internal Revenue Manual § 32.1.5.4.7.5.1(7) & (8) (Sept. 30, 2011).

e.g., *Air Transp. Ass'n of Am. v. Dep't of Transp.*, 900 F.2d 369, 379-80 (D.C. Cir. 1990) (holding final regulations invalid due to procedural failings of interim-final regulations), *vacated without opinion and remanded*, 498 U.S. 1023 (1991), *vacated as moot*, 933 F.2d 1043 (D.C. Cir. 1991); *cf. Sharon Steel Corp. v. EPA*, 597 F.2d 377, 381 (3d Cir. 1979) (holding post-promulgation notice and comment inadequate to remediate procedurally flawed final regulations). In other decisions, however, courts have declined to invalidate final regulations on such grounds, based upon a finding that the agency's handling of post-promulgation comments demonstrated an "open mind" in the process of adopting the final regulations. *See, e.g.*, *Advocates for Highway & Auto Safety v. Fed. Highway Admin.*, 28 F.3d 1288, 1292 (D.C. Cir. 1994); *Levesque v. Block*, 723 F.2d 175, 188 (1st Cir. 1983). Some courts are reluctant to undo agency regulations where doing so will yield no substantive difference. *See, e.g.*, *U.S. Steel Corp. v. EPA*, 605 F.2d 283, 291 (7th Cir. 1979). Other courts are more concerned that allowing post-promulgation notice and comment to cure the procedural flaws of temporary regulations eviscerates the notice and comment requirements of APA § 553. *See, e.g.*, *Natural Res. Def. Council, Inc. v. EPA*, 683 F.2d 752, 768 (3d Cir. 1982); *Sharon Steel Corp.*, 597 F.2d at 381 ("If a period for comments after issuance of a rule could cure a violation of the APA's requirements, an agency could negate at will the Congressional decision that notice and an opportunity for comment must precede promulgation.").

As a practical matter, the Court should be wary of taking too hard a line against interim-final rulemaking in the absence of a statutory exception from APA § 553. The procedural flaw that afflicts Treas. Reg. § 301.6501(e)-1 is not isolated to one or even a small number of regulations. Treasury has been issuing temporary regulations with only post-promulgation notice and comment and without contemporaneous good cause claims for three decades. In one relatively recent three-year period, Treasury issued temporary regulations in 84 of 232—or 36.2%—of regulation projects undertaken. *See* Hickman, *Coloring Outside the Lines*, *supra*, at 1748-49. Hundreds of Treasury regulations currently on the books could be endangered if the Court were to adopt a strict compliance model, and the tax system would be thrown into chaos to the undoubted detriment of taxpayers. Other areas of law might suffer similarly, as many other agencies employ interim-final rulemaking; presumably at least some of those efforts are premised on flawed assertions of good cause or another exception from APA § 553. *See* Asimow, *Interim-Final Rules*, *supra*, at 712-15 (counting interim-final rules published in the Federal Register and the agencies publishing them over time).

Furthermore, agencies that employ temporary or interim-final rules with post-promulgation notice and comment often do so based on claims of good cause or other exceptions that they believe in good faith to be valid and that only later prove to be flawed. In many instances, invalidating final regulations for the procedural flaws of their temporary predecessors will often be wasteful and

create unnecessary uncertainty in the law with no substantial apparent payoff for regulated parties. Particularly where an agency can demonstrate that it approached public comments with an open mind, invalidating a final regulation for the procedural flaws of its temporary predecessor may seem more arbitrary to regulated parties than the agency's failure to comply precisely with the terms of APA § 553.

At the same time, the Court should not simply permit agencies to ignore the terms of APA § 553 without consequence. Pre-promulgation public notice and opportunity for comment plays an important role in enhancing the legitimacy of agency rulemaking. If the Court consents entirely to agency uses of interim-final rulemaking that lack a valid exception from APA § 553, then agencies will have the power to act with the force of law and bind the actions of regulated parties for months or years without first pursuing public notice and comment, and Congress's goals for APA § 553 will be subverted.

Hence, as a general matter, a middle path based on some version of the open mind standard may ultimately prove to be the best alternative. *See, e.g.*, *Levesque v. Block*, 723 F.2d 175, 187-88 (2d Cir. 1983) (discussing and comparing the costs of interim-final rulemaking with the benefits of the open mind standard). The instruction in APA § 706 that reviewing courts take "due account . . . of the rule of prejudicial error" may offer a textual anchor for an open mind standard for evaluating interim-final rulemaking where no statutory exception from APA § 553 applies. 5 U.S.C. § 706. That said, the Court

need not resolve fully the parameters of such a compromise approach in this case, for the circumstances of Treas. Reg. § 301.6501(e)-1 should render it ineligible for leniency.

Where, as here, an agency adopts a procedurally invalid temporary or interim-final rule in the midst of litigation, the Court ought not to allow the final replacement of that rule to stand. The combination of ongoing litigation and a procedurally invalid temporary or interim-final rule is simply irreconcilable with the goal of meaningful public participation, as this case demonstrates.

In this instance, Treasury issued Temp. Treas. Reg. § 301.6501(e)-1T and its corresponding notice of proposed rulemaking in the midst of a protracted and very public litigation battle over the meaning of IRC § 6501(e). At the time that Treasury issued its temporary and proposed regulations, at least two circuit courts of appeals had rejected its interpretation in light of this Court's decision in *Colony v. Comm'r*, 357 U.S. 28 (1958). Not only had the IRS vowed to soldier on, but Treasury was quite explicit in the preamble to Temp. Treas. Reg. § 301.6501(e)-1 regarding the agency's disagreement with the adverse circuit court opinions and its goal of using the temporary regulations to obtain *Chevron* deference for its own view. *See* T.D. 9466, 74 Fed. Reg. 49321, 49321-22 (Sept. 28, 2009). IRS Associate Chief Counsel Deborah Butler was quoted as promising publicly that the government would seek reconsideration in some cases and appeal others based on the newly-issued temporary regulations. *See* Jeremiah Coder, *IRS Strikes Back Against*

Judicial Losses in Overstated Basis Cases, 125 Tax Notes 19 (Oct. 5, 2009). The government has observed that Treasury received only a single comment concerning the regulation's retroactive effect in response to its notice of proposed rulemaking, (Gov't. Br. at 29), meaning that Treasury received no comments at all regarding the wisdom or the substantive validity of extending the six-year statute of limitations to encompass basis overstatements. The Court should not take the paucity of comments in this instance as suggesting a lack of interest in or controversy surrounding Treasury's actions. In fact, shortly after announcing Temp. Treas. Reg. § 301.6501(e)-1T, Deborah Butler was also quoted acknowledging, "We anticipate controversy," and the temporary regulations were in fact highly controversial. Coder, *supra*, at 19 (reporting comments and reactions thereto). Instead, the Court should appreciate the lack of public participation in Treasury's rulemaking process as reflecting the tax community's lack of faith that such participation would be meaningful. Subsequent comments by Deborah Butler at another American Bar Association Tax Section meeting, delivered after the Tax Court invalidated Temp. Treas. Reg. § 301.6501(e)-1 and before Treasury issued its final regulation, aptly reflect the tax community's perception of Treasury's attitude toward the regulatory process: that judicial rejections of the IRS's preferred interpretation of IRC § 6501(e) would not change the agency's view, that the agency was committed to "a long haul to get to the right answer" and that the IRS would continue to litigate until it obtained "the right answer." Jeremiah Coder, *IRS Undeterred After Tax Court's Intermountain Decision*,

127 Tax Notes 729 (May 17, 2010) (reporting comments).

Any agency in the midst of litigation will have a difficult time convincing regulated parties that it approached notice-and-comment rulemaking fairly. Where, as here, the agency compounds a perception of intransigence by improperly postponing notice and comment in its quest to win, the courts ought to consider the agency hopelessly compromised.

II. THE COURT SHOULD NOT EXTEND *CHEVRON* DEFERENCE TO AGENCY REGULATIONS PROMULGATED IN VIOLATION OF CONGRESSIONALLY IMPOSED PROCEDURAL REQUIREMENTS.

A second question raised by this case concerns the relationship between procedural compliance and *Chevron* deference. In several cases regarding the scope of IRC § 6501(e), the significance of Treasury's procedural noncompliance for judicial review under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 465 U.S. 837 (1984), has generated disagreement and confusion among the litigants and the lower courts. In particular, the Fifth Circuit has suggested that, if IRC § 6501(e) were ambiguous, then Treasury's failure to comply with APA § 553 might mean that Treas. Reg. § 301.6501(e)-1 should be denied *Chevron* deference. *See Burks v. United States*, 633 F.3d 347, 360-61 n.9 (5th Cir. 2011). The Seventh Circuit, by contrast, has suggested its inclination to give *Chevron* deference to both temporary Treasury regulations and their final replacements, notwithstanding their arguable procedural invalidity. *See Comm'r v. Beard*, 633 F.3d

616, 623 (7th Cir. 2011). This case thus offers the Court an opportunity to clarify the extent to which *Chevron* step two and procedural compliance are related.

In *United States v. Mead Corp.*, 533 U.S. 218 (2001), this Court made clear that a lack of public notice and comment, by itself, would not leave agency action ineligible for *Chevron* review. *Id.* at 230-31. This conclusion is consistent with the standard articulated in *Mead* of looking to whether agency action carries the force of law. Congress may include language in a statute authorizing agency rules with the force of law but modifying the terms of APA § 553 in that context. *See, e.g., Asiana Airlines v. FAA*, 134 F.3d 393, 398 (D.C. Cir. 1998). The APA itself authorizes legislative rules without notice and comment upon a contemporaneous and valid assertion of the good cause exception. *See* 5. U.S.C. § 553(b)(B).

Likewise, the Court has sometimes declined to deny *Chevron* deference to regulations merely because the agency adopted them in the midst of ongoing litigation. *See, e.g., Mayo Foundation for Medical Education and Research v. United States*, 131 S.Ct. 704, 712-13 (2011); *Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 740 (1996). In both of these cases, however, the Court observed that the agency adopted the regulation granted *Chevron* deference using the full notice-and-comment rulemaking procedures mandated by Congress. *See Mayo*, 131 S.Ct. at 714; *Smiley*, 517 U.S. at 741.

The Court has also suggested that, in evaluating the reasonableness of agency action at

Chevron step two, the Court's inquiry encompasses questions of broader compliance with the APA. For example, the Court just this month indicated that process review under *Motor Vehicle Mfrs. Ass'n of United States, Inc. v. State Farm Mut. Automobile Ins. Co.*, 463 U.S. 29 (1983), and *Chevron* step two analysis are "the same" because both represent variations of the arbitrary and capricious standard of APA § 706(2)(A). *See Judulang v. Holder*, No. 10-694, Slip. Op. at 9 n.7, 2011 WL 6141311 (U.S. Dec. 12, 2011); *see also, e.g., National Ass'n of Regulatory Utility Comm'rs v. ICC*, 41 F.3d 721 (D.C. Cir. 1994) (noting that "the inquiry at the second step of *Chevron* overlaps analytically with a court's task under the [APA] . . . in determining whether agency action is arbitrary and capricious (unreasonable)"); Ronald M. Levin, *The Anatomy of* Chevron*: Step Two Reconsidered*, 72 Chi-Kent L. Rev. 1253, 1285-86 (1997) (advocating a merger of *Chevron* step two and process review under *State Farm* based on analysis of D.C. Circuit jurisprudence).

Although APA § 706(2)(D) specifically instructs reviewing courts to invalidate regulations that fail to comply with statutory procedures, APA § 706(2)(A) correspondingly compels reviewing courts to set aside regulations found to be "arbitrary, capricious, an abuse of discretion, or *otherwise not in accordance with law*." 5 U.S.C. § 706(2)(A) (emphasis added). Failing to comply with congressionally-mandated procedural requirements, whether found in APA § 553(b) or elsewhere, is obviously not in accordance with law. Treas. Reg. § 301.6501(e)-1 was adopted in the midst of litigation using procedures other than those mandated by Congress. As a result, *Chevron*

deference should not be available to Treas. Reg. § 301.6501(e)-1 given the circumstances of its issuance.

CONCLUSION

Tax shelters are a scourge. One does not need to be tremendously sympathetic to tax collectors to recognize that tax shelters undermine the viability of the federal tax system. Not everyone agrees which transactions are or are not tax shelters, but few would argue that the Son-of-BOSS transaction is not a tax shelter. Moreover, Treas. Reg. § 301.6501(e)-1 reaches many more taxpayers than merely tax shelter participants. Nevertheless, in its war against tax shelters, Treasury has itself gone too far in pushing the limits of the law. Treasury's failure to comply with the procedural requirements that Congress has imposed upon it is just as corrosive to the tax system as the behavior of tax shelter rogues. For all of the reasons stated above, in the interest of preserving taxpayer confidence in Treasury's fairness in administering the tax system, the Court should invalidate Treas. Reg. § 301.6501(e)-1.

Respectfully submitted,

Prof. Kristin E. Hickman
Amicus Curiae and Counsel of Record
University of Minnesota Law School
229 19th Avenue South
Minneapolis, MN 55455
(612) 624-2915
khickman@umn.edu

December 22, 2011

AMICUS CURIAE BRIEF

No. 11-139

IN THE
SUPREME COURT OF THE UNITED STATES

UNITED STATES,
Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF OF *AMICUS CURIAE* NATIONAL ASSOCIATION OF HOME BUILDERS IN SUPPORT OF RESPONDENTS

CHRISTOPHER M. WHITCOMB*
NATIONAL ASSOCIATION OF HOME BUILDERS
1201 15TH STREET, N.W.
WASHINGTON, D.C. 20005
(202) 266-8329
cwhitcomb@nahb.org

*Counsel of Record

December 22, 2011

QUESTION PRESENTED

Whether a final regulation promulgated by the Department of the Treasury, which reflects the IRS's view that an understatement of gross income attributable to an overstatement of basis can trigger the extended six-year assessment period, is entitled to judicial deference.

TABLE OF CONTENTS

Page(s)

QUESTION PRESENTED i

INTEREST OF THE *AMICUS CURIAE* 1

SUMMARY OF ARGUMENT 3

ARGUMENT 4

I. *Post Hoc* Rationalization of the IRS's Litigating Position Does Not Draw *Chevron* Deference 4

II. The Court Should Clarify *Brand X* 9

III. The Regulation Should Be Invalidated Because it Failed to Allow for Proper Notice Under the Administrative Procedure Act 11

CONCLUSION 16

TABLE OF AUTHORITIES

Page(s)

Cases

Am. Bar Ass'n v. Federal Trade Comm'n, 430 F.3d 457 (D.C. Cir. 2005) 5

Am. Mining Cong. v. Mine Safety & Health Admin., 995 F.2d 1106 (D.C. Cir. 1993) 11-12

Am. Standard, Inc. v. United States, 602 F.2d 256 (Cl. Ct. 1979) 15

Bowen v. Georgetown Univ. Hosp. et al., 488 U.S. 204 (1988) 4

Burks v. United States, 633 F.3d 347 (5th Cir. 2011) 6, 13

Caterpillar Tractor Co. v. United States, 589 F.2d 1040 (Cl. Ct. 1978) 5

Chevron U.S.A., Inc. *v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984) ..... *passim*

Chock Full O'Nuts Corp. v. United States, 453 F.2d 300 (2d Cir. 1971) 5

Chrysler Corp. v. Brown, 441 U.S. 281 (1979) 11

Citizens to Pres. Overton Park, Inc. v. Volpe, 401 U.S. 402 (1971) 5

City of Kansas City, Mo. v. Dep't of Hous. & Urban Dev., 923 F.2d 188 (D.C. Cir. 1991) 4

Colony, Inc. v. C.I.R., 357 U.S. 28 (1958) 3, 9

TABLE OF AUTHORITIES *(cont.)*

Page*(s)*

Cont'l Oil Co. v. Burns, 317 F. Supp. 194 (D. Del. 1970) 14

CropLife Am. v. EPA, 329 F.3d 876 (D.C. Cir. 2003) 12

Fed. Labor Relations Auth. v. U.S. Dept. of Navy, 966 F.2d 747 (3d Cir. 1992) 12

Gibson Wine Co. v. Snyder, 194 F.2d 329 (D.C. Cir. 1952) 11

Gen. Elec. Co. v. E.P.A., 290 F.3d 377 (D.C. Cir. 2002) 12, 14

Gen. Motors Corp. v. Ruckelhaus, 742 F.2d 1561 (D.C. Cir. 1984) 11

Hernandez-Carrera v. Carlson, 547 F.3d 1237 (10th Cir. 2008) 10

Intermountain Ins. Serv. of Vail, Ltd. Liab. Co. v. C.I.R., 134 T.C. 211 (T.C. 2010), *rev'd*, 650 F.3d 691 (D.C. Cir. 2011) 6

Int'l Union, United Mine Workers of Am. v. Mine Safety & Health Admin., 407 F.3d 1250 (D.C. Cir. 2005) 13-14

Long Island Care At Home, Ltd., et al. v. Coke, 551 U.S. 158 (2007) 8

Mayo Found. for Med. Research v. United States, 131 S.Ct. 704 (2011) 6

Mercado-Zazueta v. Holder, 580 F.3d 1102 (9th Cir. 2009) 9

TABLE OF AUTHORITIES *(cont.)*

Page*(s)*

Mt. Diablo Hosp. Dist., et al. v. Bowen, 860 F.2d 951 (9th Cir. 1988) 12

NAHB v. Defenders of Wildlife, 551 U.S. 644 (2007) 1-2

NAHB v. U.S. Army Corps of Eng'rs, 539 F.Supp.2d 331 (D.D.C. 2008) 7

NAHB v. U.S. Army Corps of Eng'rs, 699 F.Supp.2d 209 (D.D.C. 2010), *vacated*, 2011 WL 6266071 (D.C. Cir. 2011) 8

Nat'l Cable and Telecomm. Ass'n v. Brand X Internet Serv., 545 U.S. 967 (2005) 3, 9, 10

Perales v. Sullivan, 948 F.2d 1348 (2d Cir. 1991) 11

SEC v. Chenery Corp., 318 U.S. 80 (1943) 4

Securities Indus. Ass'n et al. v. Bd. Of Governors of the Fed. Reserve Sys., 468 U.S. 137 (1984) 5

Smiley v. Citibank (South Dakota), N.A., 517 U.S. 735 (1996) 6, 8

Tran v. Mukasey, 515 F.3d 478 (5th Cir. 2008) .. 10

Tuan Thai v. Ashcroft, 366 F.3d 790 (9th Cir. 2004) 10

United States v. Mead Corp., 533 U.S. 218 (2001) 13

TABLE OF AUTHORITIES *(cont.)*

Page*(s)*

REGULATORY, CONSTITUTIONAL AND STATUTORY PROVISIONS

5 U.S.C. § 553 ..... 11, 12

5 U.S.C. 553(b)(A). 14

26 U.S.C. § 6501(e)(1)(A) 4, 9

26 U.S.C.A. § 275(c) 9

74 Fed. Reg. 17,456 (Apr. 15, 2009)..... 7

75 Fed. Reg. 78,897 (Dec. 17, 2010)..... 11

Treas. Reg. § 301.6501(e)-1..... 4, 9, 11

Treas. Reg. § 301.6501(e)-1T 4, 11

OTHER

Robin Kundis Craig, *Agencies Interpreting Courts Interpreting Statutes: The Deference Conundrum of a Divided Supreme Court*, 61 Emory L. J. 1 (2011) 9

Kristin E. Hickman, *A Problem of Remedy: Responding to Treasury's (Lack Of) Compliance With Administrative Procedure Act Rulemaking Requirements*, 76 Geo. Wash. L. Rev. 1153 (August, 2008) 3

Steve R. Johnson, *Intermountain and the Growing Importance of Administrative Law in Tax Law*, 128 Tax Notes 837 (August 23, 2010)..... 14

Andrew Pruitt, *Judicial Deference to Retroactive Interpretative Treasury Regulations*, 79 Geo. Wash. L. Rev. 1558 (July, 2011) 7

INTEREST OF THE *AMICUS CURIAE*

The National Association of Home Builders ("NAHB") has received the parties' written consent to file this *amicus curiae* brief in support of the Respondent.[1] NAHB is a Washington, D.C.-based trade association whose mission is to enhance the climate for housing and the building industry. Chief among NAHB's goals is providing and expanding opportunities for all people to safe, decent and affordable housing. As the voice of America's housing industry, NAHB promotes policies that keep housing a national priority. Founded in 1942, NAHB is a federation of more than 800 state and local associations. About one-third of NAHB's 160,000 members are home builders or remodelers. These members build about 80 percent of the new homes constructed each year in the United States. The remaining members are associates working in closely related fields within the housing industry, such as mortgage finance and building products and services.

Where appropriate, NAHB is a vigilant advocate in the nation's courts. It frequently participates as a party litigant and *amicus curiae* to safeguard the property rights and, interests of its members. NAHB was a petitioner in *NAHB v. Defenders of*

---

1 All letters of consent are on file with the Clerk. Under Rule 37.6 of the Rules of this Courts Amicus states that no counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amici curiae*, its members, or its counsel made a monetary contribution to its preparation or submission.

Wildlife, 551 U.S. 644 (2007). It also has participated before this Court as *amicus curiae* or "of counsel" in a number of cases involving landowners aggrieved by excessive regulation under a wide array of statutes and regulatory programs. *See* Appendix A.

NAHB's organizational policies have long advocated the importance of the Administrative Procedure Act in the development of regulatory policy. NAHB's members frequently face potentially costly regulation from a variety of federal agencies. For that reason, it is vital for the industry to maintain its ability to communicate concerns over the impact of proposed regulations before they take effect. In addition, NAHB's members often confront agencies that attempt to circumvent the APA's notice-and-comment requirements.

SUMMARY OF ARGUMENT

This controversy implicates fundamental issues involving the interplay between judicial deference and the Administrative Procedure Act ("APA"). The Internal Revenue Service ("IRS") asks this Court to uphold its use of the regulatory process to bolster its litigating position. The law prior to its action did not support its argument so the IRS issued new regulations which purported to change the law. Neither thoughtful nor principled, this trump-card view of regulatory rulemaking turns precedent on its head.

If the Regulations are upheld, they would also overturn the Court's decision in *Colony, Inc. v. Comm'r of Internal Revenue*, 357 U.S. 28 (1958), implicating the issue of whether deference is appropriate when an administrative agency promulgates a regulation in conflict with the Court's own precedent. *See Nat'l Cable and Telecomm. Ass'n v. Brand X Internet Serv.*, 545 U.S. 967 (2005).

Ultimately, the Regulations are emblematic of the IRS's lackadaisical attitude toward the notice-and-comment requirements. The manner in which the IRS issued the Temporary Regulation here "follow[ed] a pattern of . . . impos[ing] a legal burden upon taxpayers to conform to regulations before submitting those regulations for public comment." Kristin E. Hickman, *A Problem of Remedy: Responding to Treasury's (Lack Of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 76 Geo. Wash. L. Rev. 1153, 1160 (August, 2008). This process is further exacerbated in this case by the fact that the IRS imposed that

burden merely to trump opposing parties' arguments in court.

ARGUMENT

I. *Post Hoc* Rationalization of the IRS's Litigating Position Does Not Draw *Chevron* Deference

The IRS issued both Treas. Reg. § 301.6501(e)-1T and Treas. Reg. § 301.6501(e)-1 in the midst of litigating the very same issue the Regulations address—whether an overstated basis is an omission from gross income under 26 U.S.C. § 6501(e)(1)(A). Because the Regulations represent a *post hoc* rationalization for the purpose of strengthening the IRS's litigating position, they should not be afforded deference under *Chevron, U.S.A.*, Inc. *v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (1984).

The Court has explained that it can only uphold the decision of an administrative agency on the basis "upon which the record discloses that its action was based." *SEC v. Chenery Corp.*, 318 U.S. 80, 87 (1943). Under this analysis, courts have established that *Chevron* deference is not applicable where a regulation is adopted solely in response to litigation. "[D]eference to what appears to be nothing more than an agency's convenient litigating position would be entirely inappropriate." *Bowen v. Georgetown Univ. Hosp. et al.*, 488 U.S. 204, 213 (1988). The District of Columbia Circuit has been similarly explicit in this regard, warning against deference where prevailing in litigation is the primary motivation. *See City of Kansas City, Mo. v. Dep't of Hous. & Urban Dev.*, 923 F.2d 188, 192 (D.C. Cir. 1991) ("In whatever context we defer to agencies, we

do so with the understanding that the object of our deference is the result of agency decisionmaking, and not some *post hoc* rationale developed as part of a litigation strategy.").[2]

Federal courts have applied this principle in the context of Treasury and IRS rulemakings. The Court of Federal Claims explained that a "regulation is invalid as to the taxpayer if the Treasury has abused its discretion . . . to adopt a regulation with the purpose of aiding pending litigation." *Caterpillar Tractor Co. v. United States*, 589 F.2d 1040, 1043 (Cl. Ct. 1978) (finding no evidence that the regulation at issue was adopted to aid pending litigation). In the same vein, the Second Circuit explained that the IRS "may not take advantage of [its] power to promulgate retroactive regulations during the course of a litigation for the purpose of providing [itself] with a defense based on the presumption of validity accorded to such regulations." *Chock Full O'Nuts Corp. v. United States*, 453 F.2d 300, 303 (2d Cir. 1971).

Decisions by courts below in both this case and the related litigation evidence their suspicion and discomfort with the tactic used by the IRS in this case. The Tax Court, in part, refused to grant deference to the government because the Temporary

---

2 *See also, Securities Indus. Assoc. et al. v. Bd. Of Governors of the Fed. Reserve Sys.*, 468 U.S. 137, 143 (1984) (finding that *post hoc* rationalizations about regulations during litigation are entitled to little deference); *Citizens to Pres. Overton Park, Inc. v. Volpe*, 401 U.S. 402 (1971); *Am. Bar Ass'n v. Fed. Trade Comm'n*, 430 F.3d 457, 471 (D.C. Cir. 2005) ("[W]e cannot affirm an agency's actions based on the *post hoc* rationale of its litigating position.").

Regulation was "irreparably marred by circular, result-driven logic". *Intermountain Ins. Serv. of Vail, Ltd. Liab. Co. v. C.I.R.*, 134 T.C. 211, 219 (T.C. 2010), *rev'd*, 650 F.3d 691 (D.C. Cir. 2011).

Similarly, the Fifth Circuit noted that this Court has looked unfavorably upon attempts to use the regulatory process as a litigating tool. *See Burks v. United States*, 633 F.3d 347, 360 n. 9 (5th Cir. 2011). In support of its conclusion, the Fifth Circuit relied on the fact that in *Mayo Found. for Med. Research v. United States*, 131 S.Ct. 704 (2011), this Court "was not faced with a situation where, during the pendency of the suit, the treasury promulgated determinative, retroactive regulations following prior adverse judicial decisions on the identical legal issue." 633 F.3d at 360 n.9.

The manner in which the IRS adopted the Regulations can also be contrasted to this Court's past explanations regarding the interplay between the regulatory process and pending litigation. In *Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735 (1996), the Court reiterated *Bowen's* holding that deference is not due to "wholly unsupported" litigating positions and explained that "[t]he deliberateness of such positions, if not indeed their authoritativeness, is suspect." *Id.* at 741. Notably, in *Smiley* the Court found the fact that the agency had gone through the full regulatory process, including notice and comment, to be compelling. *Id.* It is also notable that, in *Smiley*, the Office of the Comptroller of the Currency was not a party to the litigation. The court concluded that the agency's compliance with the APA made it unlikely that the issuance of a regulation would have an unfair result,

even though it occurred during the pendency of litigation.

Indeed, commentators have noted that "[t]he IRS's manifest purpose in the Intermountain cases is to introduce policy interpretations post hoc into actively litigated issues to upset court decisions." Andrew Pruitt, *Judicial Deference to Retroactive Interpretative Treasury Regulations*, 79 Geo. Wash. L. Rev. 1558, 1582 (July, 2011). This type of agency "action" is nothing more than a reincorporation of its unsuccessful litigating position into a legislative regulation. "The caselaw on judicial deference does not permit the use of regulatory powers to interfere with ongoing litigation or to upset decided cases." *Id.*

Attempted use of the regulatory process by agencies as a trump card in litigation is neither new nor limited to the IRS. In fact, the U.S. Army Corps of Engineers ("the Corps") recently undermined a district court's decision to uphold standing for certain plaintiffs to seek judicial review under the Clean Water Act. *See NAHB v. U.S. Army Corps of Eng'rs*, 539 F.Supp.2d 331 (D.D.C. 2008). After the court upheld the ability of private parties to challenge the Corps' Nationwide Permits, it issued a Notice that eliminated standing for the same type of plaintiffs involved in the underlying litigation. *See* 74 Fed Reg. 17,456, 17,457.

The Corps explicitly undermined the plaintiff's standing to challenge the permit by claiming that applicants who "voluntarily choose to seek" coverage under the permit should fail. *Id.* Thus, the notice was aimed to extra-judicially affect the outcome of ongoing litigation by amending its administrative

record after the fact. Ultimately, the district court ignored the Corps' tactic, upholding its prior decision. *NAHB v. U.S. Army Corps of Eng'rs*, 699 F.Supp.2d 209 (D.D.C. 2010), *vacated*, 2011 WL 6266071 (D.C. Cir. 2011).

The parallels to the IRS's litigation driven regulation in this case are striking. Both agencies sought to permanently alter judicial precedent by removing potential claims and defenses. Taxpayers in the instant case were suddenly faced with the elimination of a defense by regulatory fiat. The Corps similarly used its federal rulemaking authority to strip an entire class of plaintiffs of the constitutional ability to challenge that agency's action in court.

Courts have been justifiably suspicious of attempts by agencies to use regulatory powers to influence the outcome of litigation in this way. Of course, the mere existence of litigation in connection with a rulemaking cannot eliminate *Chevron* deference. *See Long Island Care At Home, Ltd., et al. v. Coke*, 551 U.S. 158, 159-160 (2007) ("where . . . an agency's course of action indicates that its interpretation of its own regulation reflects its considered views on the matter in question . . . there is no reason to suspect that its interpretation is merely a *post hoc* rationalization."). As in *Smiley*, the U.S. Department of Labor was not a party to the litigation in this case.

But where a regulation is brought solely to influence litigation, and is unsupported by existing statute or regulation, applying *Chevron* deference would turn a blind eye to reality. An agency cannot

reformat a brief as a regulation and thereby win a losing case.

II. The Court Should Clarify *Brand X*

In *Brand X*, 545 U.S. 967 (2005), the Court explained the deference to be given agency rulemakings that conflict with lower court decisions. Under *Brand X*, an agency's statutory construction is entitled to *Chevron* deference despite a contrary judicial construction unless the court found the statute unambiguous. *Id.* at 982.

In *Colony*, 357 U.S. 28 (1958), the Court determined that an overstated basis did not constitute an omission from gross income under former § 275(c), the predecessor to § 6501(e)(1)(A). *Id.* at 37. Further, the Court stated that its conclusion was "In harmony with the unambiguous language of § 6501(e)(1)(A)". *Id.* Thus, Treas. Reg. § 301.6501(e)-1 does not appear entitled to *Chevron* deference under the Court's analysis in *Brand X* because its own prior decision found the statute at issue here unambiguous.

In any event, "if the judicial precedent at issue fully addressed the agency's proffered interpretation, an agency cannot use *Brand X* to circumvent the court's prior resolution." Robin Kundis Craig, *Agencies Interpreting Courts Interpreting Statutes: The Deference Conundrum of a Divided Supreme Court*, 61 Emory L. J. 1, 21 (2011); *see also, Mercado-Zazueta v. Holder*, 580 F.3d 1102 (9th Cir. 2009) (holding *Brand X* did not apply because the court had previously considered agency's position through a *Chevron* analysis).

This case thus presents an opportunity for the Court to address the unresolved issue of whether *Brand X* applies to its own precedent. In the *Brand X* decision, Justice Stevens left the door open to a different standard for the Court's own precedent, stating that the case "would not necessarily be applicable to a decision by this Court that would presumably remove any pre-existing ambiguity." 545 U.S. at 1003.

Because the Court has not spoken directly to this issue, circuit courts have wrestled with regulatory positions that conflict with the Court's precedent. The Tenth Circuit explicitly applied *Brand X* to Supreme Court holdings, explaining that "we see no reason why the holding in *Brand X* would not be equally applicable to agency constructions that displace tentative Supreme Court interpretations." *Hernandez-Carrera v. Carlson*, 547 F.3d 1237, 1247 (10th Cir. 2008). The court dismissed Justice Stevens' concurrence, and determined that *Brand X* must apply to both lower court and Supreme Court decisions in order to be consistent. *Id.* The court, however, acknowledged that this principle conflicted with decisions from both the Fifth Circuit and Ninth Circuit, which applied Supreme Court precedent as definitive statutory interpretations. *See Tran v. Mukasey*, 515 F.3d 478 (5th Cir. 2008); *Tuan Thai v. Ashcroft*, 366 F.3d 790 (9th Cir. 2004).

The Court should eliminate the confusion in the lower courts over the application of *Brand X*. A fuller explanation of the interplay between Supreme Court statutory construction and agency rulemaking would benefit both the regulated community and federal agencies.

III. The Regulation Should Be Invalidated Because it Failed to Allow for Proper Notice Under the Administrative Procedure Act

Closely related to the availability of *Chevron* deference is whether the IRS complied with notice and comment requirements under the APA when it issued Treas. Reg. § 301.6501(e)-1T and Treas. Reg. § 301.6501(e)-1. Because the Regulations were made immediately effective and retroactive, it did not allow for meaningful notice and comment under the APA. *See* 5 U.S.C. § 553. Indicative of the adequacy of the notice (or, more accurately, the IRS's receptivity to comment), the final regulation was published without material change. 75 Fed. Reg. 78,897 (Dec. 17, 2010).

Courts have long held that a substantive regulation is subject to the procedural requirements of § 553 when it grants rights, imposes obligations, or substantially effects private parties. *See Perales v. Sullivan*, 948 F.2d 1348 (2d Cir. 1991). Courts have firmly established that when an agency action intends to create new law, rights, or duties, a legislative rule results because it has the force of law. *See, e.g. Chrysler Corp. v. Brown*, 441 U.S. 281, 302-03 (1979), *Gibson Wine Co. v. Snyder*, 194 F.2d 329, 331 (D.C. Cir. 1952) (holding that legislative rules are those which create law); *Gen. Motors Corp. v. Ruckelhaus*, 742 F.2d 1561, 1565 (D.C. Cir. 1984) (en banc) (a legislative rule exists where "the agency intends to create new law, rights or duties.").[3] In

---

3 The D.C. Circuit has explained that rules have the force of law when any of the following factors are met: "(1) whether

contrast, interpretive rules are those that assert an agency's construction of a statute and do not carry the force and effect of law. *See Fed. Labor Relations Auth. v. U.S. Dept. of Navy*, 966 F.2d 747 (3d Cir. 1992).

Courts have readily applied this analysis to Treasury Regulations and other IRS guidance. In *Mt. Diablo Hosp. Dist., et al. v. Bowen*, 860 F.2d 951 (9th Cir. 1988), the IRS issued a new policy on Medicare bonuses under the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") without conducting a rulemaking under § 553. The court noted that "[t]he label an agency gives to a particular statement of policy is not dispositive." *Id.* at 956; *see also, CropLife Am. v. E.P.A.*, 329 F.3d 876, 883 (D.C. Cir. 2003) ("[T]he agency's characterization of its own action is not controlling if it self-servingly disclaims any intention to create a rule with the 'force of law'.") *citing Gen. Elec. Co. v. E.P.A.*, 290 F.3d 377, 385 (D.C. Cir. 2002).

Continuing, the court held that because the new policy changed how reimbursement was to be determined under TEFRA, it represented "a change in law and policy that must be promulgated

---

in the absence of the rule there would not be an adequate legislative basis for enforcement action or other agency action to confer benefits or ensure the performance of duties, (2) whether the agency has published the rule in the Code of Federal Regulations, (3) whether the agency has explicitly invoked its general legislative authority, or (4) whether the rule effectively amends a prior legislative rule." *Am. Mining Cong. v. Mine Safety & Health Admin.*, 995 F.2d 1106, 1112 (D.C. Cir. 1993).

according to the notice and comment rulemaking." *Id.* at 958.

The need for proper notice in the context of legislative regulations is closely tied to the availability of *Chevron* deference. In fact, the Court has explained that notice-and-comment rulemaking is a strong indication that *Chevron* deference is appropriate. *See United States v. Mead Corp.*, 533 U.S. 218, 227 (2001). Commenting on this Court's *Mayo* decision, the Fifth Circuit explained the interplay:

> ". . . *Mayo* emphasized that the regulations at issue had been promulgated following notice and comment procedures . . . Legislative regulations are generally subject to notice and comment procedure pursuant to the Administrative Procedure Act . . . Here, the government issued the Temporary Regulations without subjecting them to notice and comment procedures . . "

Burks, 633 F.3d 347, 360 n. 9 (5th Cir. 2011). In other words, for improperly promulgated regulations to lack *Chevron* deference is unsurprising given the purpose behind notice-and-comment rulemaking.

In fact, legislative rules are entitled to a higher degree of deference because it is assumed that the agency has afforded affected parties a meaningful opportunity to weigh-in. The APA's notice-and-comment requirements are that opportunity. They are meant to "(1) to ensure that agency regulations are tested via exposure to diverse public comment, (2) to ensure fairness to affected parties, and (3) to give affected parties an opportunity to develop

evidence in the record to support their objections to the rule and thereby enhance the quality of judicial review." *Int'l Union, United Mine Workers of Am. v. Mine Safety & Health Admin.*, 407 F.3d 1250, 1259 (D.C. Cir. 2005). Because the Regulations at issue here frustrated all of these purposes, they should be invalidated under the APA.

Quite simply, the Regulations are a clear attempt "to make or change binding law, not merely to inform the public of Treasury's construction of the statute." Steve R. Johnson, *Intermountain and the Growing Importance of Administrative Law in Tax Law*, 128 Tax Notes 837 (August 23, 2010). While interpretive regulations are meant to clarify the application of existing law, it is only legislative regulations that are meant to create new legal requirements and overrule judicial precedent. For this reason, the Regulations should be considered a legislative rulemaking that does not qualify for the interpretive regulation exception to notice-and-comment under the APA. 5 U.S.C. 553(b)(A). And because the Regulations substantially modify existing law indeed, that was their sole purpose lack of a meaningful notice-and-comment period is fatal. This impact can be measured by "the drastic changes effected in existing law by the rules" and "the degree of retroactivity and its impact." *Cont'l Oil Co. v. Burns*, 317 F. Supp. 194, 197 (D. Del. 1970).

The remedy for a violation of the §553 of the APA is clear—invalidation of the regulation. There is ample case law to support invalidation in both tax and non-tax contexts. In *Gen. Elec. Co.*, 290 F.3d 377 (D.C. Cir. 2002), the District of Columbia Circuit held that a guidance document had the force of law

and was, therefore, a legislative regulation required to be subjected to notice-and-comment. *Id.* at 385. Because the guidance document did not follow notice-and-comment, the court invalidated it. *Id.*

Similarly, in *Am. Standard, Inc. v. United States*, 602 F.2d 256 (Cl. Ct. 1979), the United States Claims Court invalidated a Treasury Regulation because the regulation was "in violation of the delegation of rulemaking power and of the notice requirement of the Administrative Procedure Act." *Id.* at 269.

The APA's notice and comment requirements are meant to eliminate the possibility of unfair surprise and to allow the regulated community the opportunity to weigh-in on the impact of proposed regulations. While Temporary Regulations are a recognized tool for the IRS, the agency must have a justification beyond the fact that the law no longer supports the Agency's litigating position. For *Chevron* deference to be meaningful, this Court should unequivocally link the APA's notice-and-comment requirements to the underlying validity of the agency's actions.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be affirmed.

DATED: December 22, 2011.

Respectfully submitted,

CHRISTOPHER M. WHITCOMB*
NATIONAL ASSOCIATION OF
HOME BUILDERS
1201 15TH STREET, N.W.
WASHINGTON, D.C. 20005
(202) 266-8329
cwhitcomb@nahb.org

*Counsel of Record

December 22, 2011

APPENDIX A

Cases in which NAHB has appeared as an *amicus curiae* or "of counsel" before this Court include:

Agins v. City of Tiburon, 447 U.S. 255 (1980); *San Diego Gas and Elec. Co. v. City of San Diego*, 450 U.S. 621 (1981); *Williamson County Reg'l Planning Comm'n v. Hamilton Bank*, 473 U.S. 172 (1985); *MacDonald, Sommer & Frates v. Yolo County*, 477 U.S. 340 (1986); *First English Evangelical Lutheran Church v. Los Angeles County*, 482 U.S. 304 (1987); *Nollan v. Cal. Coastal Comm'n*, 483 U.S. 825 (1987); *Pennell v. City of San Jose*, 485 U.S. 1 (1988); *Yee v. City of Escondido*, 503 U.S. 519 (1992); *Lucas v. S.C. Coastal Council*, 505 U.S. 1003 (1992); *Dolan v. City of Tigard*, 512 U.S. 374 (1994); *Babbitt v. Sweet Home Chapter of Cmtys. for a Greater Ore.*, 515 U.S. 687 (1995); *Suitum v. Tahoe Reg'l Planning Agency*, 520 U.S. 725 (1997); *City of Monterey v. Del Monte Dunes at Monterey, Ltd.*, 526 U.S. 687 (1999); *Solid Waste Agency of N. Cook County v. U.S. Army Corps of Eng'rs*, 531 U.S. 159 (2001); *Palazzolo v. Rhode Island*, 533 U.S. 606 (2001); *Franconia Assocs. v. United States*, 536 U.S. 129 (2002); *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302 (2002); *Borden Ranch P'ship v. U.S. Army Corps of Eng'rs*, 537 U.S. 99 (2002); *City of Cuyahoga Falls v. Buckeye Cmty. Hope Found.*, 538 U.S. 188 (2003); *S. Fla. Water Mgmt. Dist. v. Miccosukee Tribe of Indians*, 541 U.S. 95 (2004); *San Remo Hotel, L.P. v. City and County of San Francisco*, 545 U.S. 323 (2005); *Lingle v. Chevron U.S.A., Inc.*, 544 U.S. 528 (2005); *Kelo v. City of New London*, 545 U.S. 469 (2005); *S.D. Warren Co. v. Me.*

APPENDIX A

Bd. of Envtl. Prot., 547 U.S. 370 (2006); *Rapanos v. United States*, 547 U.S. 715 (2006); *NAHB v. Defenders of Wildlife*, 55 U.S. 644 (2007); *John R. Sand and Gravel Co. v. United States*, 551 U.S. 130 (2008); *Summers v. Earth Island Inst.*, 129 S. Ct. 1142 (2009); *Entergy Corp. v. Envtl. Prot. Agency*, 129 S. Ct. 1498 (2009); and *Winter v. Natural Res. Def. Council*, 129 S. Ct. 365 (2008); *Coeur Alaska, Inc. v. Southeast Alaska Cons. Council*, 129 S. Ct. 2458 (2009); *Monsanto v. Geertson Seed Farms*, 130 S. Ct. 2743 (2010); *United States v. Tohono O'odham Nation*, 559 F.3d 1284 (Fed. Cir. 2009), *cert. granted* 130 S. Ct. 2097 (2010) (No. 09-846); *Am Elec. Power Co., Inc. v. Connecticut*, 582 F.3d 309 (2d Cir. 2009), *cert. granted*, 131 S. Ct. 813 (2010) (No. 10-174); *Sackett v. United States Envtl. Prot. Agency*, 622 F.3d 1139 (9th Cir. 2010), *cert. granted*, 2011 WL 675769 (June 28, 2011) (No. 10-1062).

AMICUS CURIAE BRIEF

No. 11-139

In The
Supreme Court of the United States

UNITED STATES OF AMERICA,
Petitioner,
v.
HOME CONCRETE & SUPPLY, LLC, *et al.*,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF *AMICI CURIAE* OF NATIONAL FEDERATION OF INDEPENDENT BUSINESS SMALL BUSINESS LEGAL CENTER AND CATO INSTITUTE IN SUPPORT OF RESPONDENTS

Elizabeth Milito
Counsel of Record
Karen R. Harned
Katherine A. Isard
NATIONAL FEDERATION OF INDEPENDENT BUSINESS SMALL BUSINESS LEGAL CENTER
1201 F Street, N.W., Suite 200
Washington, DC 20004
(202) 406-4443
elizabeth.milito@nfib.org

Ilya Shapiro
CATO INSTITUTE
1000 Mass. Ave., N.W.
Washington, D.C. 20001
(202) 842-0200
ishapiro@cato.org

Counsel for Amici Curiae

Dated: December 22, 2011

THE LEX GROUP DC • 1825 K Street, N.W. • Suite 103 • Washington, D.C. 20006
(202) 955-0001 • (800) 856-4419 • Fax: (202) 955-0022 • www.thelexgroup.com

QUESTION PRESENTED

Whether an administrative agency can change—retroactively at that—the law that Congress enacted and the Supreme Court has interpreted.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

TABLE OF CONTENTS ii

TABLE OF AUTHORITIES iii

IDENTITY AND INTEREST OF *AMICI CURIAE* 1

SUMMARY OF THE ARGUMENT 2

ARGUMENT 3

I. THE TREASURY REGULATION IS NOT ENTITLED TO *CHEVRON* DEFERENCE 3

A. THE COURT IN *COLONY* FOUND THE STATUTE TO BE UNAMBIGUOUS 5

B. THE IRS DOES NOT HAVE THE AUTHORITY TO OVERRULE SUPREME COURT PRECEDENT 7

C. DEFERENCE SHOULD NOT BE EXTENDED TO THE REGULATION UNDER *CHEVRON* STEP TWO 10

CONCLUSION 12

TABLE OF AUTHORITIES

Page(s)

CASES

Bakersfield Energy Partners, LP,
568 F.3d 767 (9th Cir. 2009)..... 4

Bowen v. Georgetown Univ. Hosp.,
488 U.S. 204, 109 S. Ct. 468 (1988)..... 11

Burks v. United States,
633 F.3d 347 (5th Cir. 2011)..... 6, 11

Carpenter Family Investments, LLC,
136 TC No. 17 (2011)..... 8

Chevron U.S.A. Inc. v.
Natural Resources Defense Council, Inc.,
467 U.S. 837 (1984).....*passim*

Chicago & Southern Air Lines, Inc. v.
Waterman S.S. Corp.,
333 U.S. 103 (1948)..... 9

Chock Full O'Nuts Corp. v. United States,
453 F.2d 300 (2d Cir. 1971)..... 11

Colony, Inc., v. Commissioner,
357 U.S. 28, 78 S. Ct. 1033 (1958).....*passim*

Home Concrete & Supply, LLC v. United States,
634 F.3d 249 (4th Cir. 2011)..... 6

Mayo Foundation for Medical Education and
Research v. United States,
131 S. Ct. 704 (2011)..... 11

Nat'l Cable & Telecomms. Ass'n v.
Brand X Internet Servs.,
545 U.S. 967 (2005)..... 4, 8, 9, 10

Neal v. United States,
516 U.S. 284 (1996).....9

Salaman Ranch Ltd.,
573 F.3d 1362 (Fed. Cir. 2009).....4

United States v. Mead Corp.,
533 U.S. 218 (2001).....10, 11

STATUTES

26 U.S.C. § 6501(a).....3

26 U.S.C. § 6501(e)(1)(A) 3, 4, 6, 11

REGULATION

Treas. Reg. § 301.6501(e)-1.....4

IDENTITY AND INTEREST OF *AMICI CURIAE*

The National Federation of Independent Business Small Business Legal Center (NFIB Legal Center)[1] is a nonprofit, public interest law firm established to provide legal resources and be the voice for small businesses in the nation's courts through representation on issues of public interest affecting small businesses. The National Federation of Independent Business (NFIB) is the nation's leading small business advocacy association, representing members in Washington, D.C., and all 50 state capitals. Founded in 1943 as a nonprofit, nonpartisan organization, NFIB's mission is to promote and protect the right of its members to own, operate, and grow their businesses. NFIB represents about 350,000 independent business owners who are located throughout the United States. The NFIB Legal Center frequently files amicus briefs in cases that will affect small businesses.

NFIB's membership includes small businesses that would be adversely affected if judicial deference is granted to a final regulation promulgated by the United States Department of the Treasury (Treasury), where the regulation is contrary to Supreme Court precedent, and was drafted during the pendency of litigation solely to revive a failing

---

[1] In accordance with Rule 37.6, *amici* state that no counsel for any party has authored this brief in whole or in part, and no person or entity, other than *amici* and its counsel has made a monetary contribution to the preparation or submission of this brief. In accordance with Rule 37.3(a), *amici* state that all parties consented to the filing of this brief. All letters of consent are on file with the Clerk.

legal position in litigation between the Internal Revenue Service (IRS) and the taxpayer. Granting deference here would severely undermine NFIB's small business members' ability to operate, in so far as they could no longer plan a regular course of business based on the consistency of the myriad of regulations applicable to each taxpayer, or rely on a fair application of current regulations or Court precedents.

The Cato Institute was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Cato's Center for Constitutional Studies was established in 1989 to promote the principles of limited constitutional government that are the foundation of liberty. Toward those ends, Cato publishes books and studies, conducts conferences, produces the annual Cato Supreme Court Review, and files amicus briefs. The present case centrally concerns Cato because the sort of ad hoc rule-making at issue here implicates constitutional separation of powers and basic rule of law principles.

SUMMARY OF THE ARGUMENT

Where Congress has not seen fit to change the meaning of a statute that has been interpreted by this Court and found to have an unambiguous meaning, it is not the role of an agency to issue a regulation purporting to change that meaning. The regulation issued here contains a directly contrary definition of a statute previously interpreted by this Court, an interpretation that has been left unchanged by Congress in the intervening decades.

The government's position is that this regulation is due judicial deference, but accepting that argument would not only contradict this Court's precedent, it would sanction an attempt to issue a new regulation *during litigation* for the purpose of reviving a failed litigation position. This argument was rejected by the lower court and if approved here would upend the constitutional balance of powers between an agency on the one hand and Congress and the Supreme Court on the other. In expounding on the deference afforded agencies pursuant to *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), and its progeny, this Court surely never intended to undermine the very structure of the Republic.

ARGUMENT

I. THE TREASURY REGULATION IS NOT ENTITLED TO *CHEVRON* DEFERENCE

There is no dispute that at the outset of this litigation, in December 2006, the three-year statute of limitations found in I.R.C. § 6501(a) applied with respect to the overstatement of basis in the 1999 tax return, timely filed by Home Concrete & Supply, LLP in April 2000. The IRS failed to act during the three-year limitations period, however, instead initiating its investigation in June 2003 and issuing a Final Partnership Administrative Adjustment (FPAA) in September 2006. The IRS similarly failed to act within the three-year time period as to several other taxpayers who had engaged in similar overstatements of basis. In each of these cases, the IRS was forced to argue for the application of the six-year statute of limitations found in § 6501(e)(1)(A),

which is applicable to situations where a taxpayer "omits from gross income" items properly included therein that constitute more than 25 percent of the gross income in the taxpayer's return.

That argument proved to be a loser for the IRS in *Bakersfield Energy Partners, LP*, 568 F.3d 767 (9th Cir. 2009) and *Salaman Ranch Ltd.*, 573 F.3d 1362 (Fed. Cir. 2009), where the Ninth and Federal Circuits applied this Court's decision in *Colony, Inc., v. Commissioner*, 357 U.S. 28, 78 S. Ct. 1033 (1958). In *Colony*, this Court interpreted the substantively identical predecessor to § 6501(e)(1)(A) to mean that an overstatement of basis was not properly included in the definition of "omits from gross income" and therefore not subject to the extended six-year statute of limitations. Although the Ninth Circuit applied *Colony* against the IRS in *Bakersfield*, it suggested that the IRS may be able, pursuant to the Court's decision in *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967 (2005) (*Brand* X), to overturn the unfavorable (to the IRS) precedent by promulgating a new regulation containing an interpretation of § 6501(e)(1)(A) that was contrary to the Court's finding in *Colony*.

The IRS quickly employed the Ninth Circuit's suggestion, issuing Proposed and Temporary Regulations on September 24, 2009, which became final Treas. Reg. § 301.6501(e)-1 on December 14, 2010 (the "Regulation"). The Regulation states, in part, that an overstatement of basis constitutes an omission from gross income for the purposes of § 6501(e)(1)(A). Though the Treasury claimed in the preamble to the Regulation, and in its arguments in this litigation, that the new regulation merely "clarifies" the meaning of § 6501(e)(1)(A), the

Regulation is a blatant attempt to overturn *Colony* and create a new statute of limitations applicable to the very litigation that prompted the Regulation.

On its face, even the six-year statute of limitations that the government argues is applicable forecloses the action taken by the IRS where, as here, more than six years have elapsed since Home Concrete filed its 1999 tax return. Therefore, beyond arguing that its regulation should receive judicial deference and overturn this Court's precedent, the IRS seeks to preserve its untimely assessment through the language added to the Regulation's preamble, which states that the six-year limitations period remains open for any litigation that was pending at the time the Regulation was promulgated. Accepting the government's arguments would effectively grant the IRS unprecedented discretion to legislate while litigating, after which a taxpayer would be subject to retroactive laws drafted by its litigation opponent and applied by courts as that opponent sees fit.

A. THE COURT IN *COLONY* FOUND THE STATUTE TO BE UNAMBIGUOUS

In *Chevron*, this Court created a two-step process for judicial review of an agency's construction of a statute that the agency is charged with administering. The first step is to determine whether the meaning of the statute is unambiguous, "for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." *Id.* at 842-43. Where Congress has spoken directly to the precise question at issue, "that is the end of the matter." *Id.* at 842. Under step two, if the

statute is ambiguous a court is to defer to an agency's "permissible construction of the statute." *Id.* at 843.

In *Colony*, this Court concluded that an overstatement of basis did not constitute an omission from gross income, and that this conclusion was "in harmony with the unambiguous language of section § 6501(e)(1)(A)." 357 U.S. at 37. Although *Colony* was decided pre-*Chevron*, it is possible to analyze that decision under the *Chevron* framework. In doing so, courts, including the circuit court here, have correctly determined that *Colony* was decided under *Chevron*'s step one. *See Burks v. United States*, 633 F.3d 347, 360 (5th Cir. 2011) (unambiguous at *Chevron* step one); *Home Concrete & Supply, LLC v. United States*, 634 F.3d 249, 257 (4th Cir. 2011) (citing *Colony*, and stating, "The Supreme Court's reference to 'the *unambiguous* language of section 6501(e)(1)(A)' cannot be ignored."). The *Colony* Court analyzed the statute using traditional means of statutory construction, looking to the plain language of the statute and legislative history. After doing so, and finding the statute to have an unambiguous meaning, that pre-*Chevron* Court effectively completed the analysis under a *Chevron* framework. Accordingly, the contrary construction set forth in the Regulation here is not entitled to deference.

The government argues that the Court in *Colony* in fact found the language "omits from gross income" to be "ambiguous" and, in support of this argument, cites the Court's statement that "it cannot be said that the [relevant] language is unambiguous." Pet'r's Br. 48, 50 (citing *Colony*, 357 U.S. at 33). The Court in *Colony* authored its

opinion 26 years before *Chevron* was decided, however, and its use of the term "ambiguous" must be taken in context. To focus on this phrase in *Colony* ignores the Court's next step, which was to review the plain language and legislative history of the statute—the same steps it would undertake today under *Chevron* step one. The *Colony* Court then concluded that based on the statutes' plain meaning, and Congressional intent, there was only one clear meaning of the term "omits from gross income." 357 U.S. at 33-35. In a post-*Chevron* world, this conclusion would end the statutory interpretation at step one, with a determination that the statute is unambiguous. Significantly, the clear meaning of the statute found by the *Colony* court is one that, in the intervening decades since the *Colony* decision, Congress has not attempted to alter.

Accordingly, *Chevron* step one requires that this Court give effect to Congress's clear intent, as determined by its own precedent, and refuse the contrary interpretation of the statute promulgated by the government.

B. THE IRS DOES NOT HAVE THE AUTHORITY TO OVERRULE SUPREME COURT PRECEDENT

The government can cite no authority for the proposition that this Court must give controlling deference to Treasury regulations in direct conflict with Court precedent—much less where that precedent determined the plain meaning of a statute. In fact, under *Chevron*, when the Court has previously determined that the statute has an unambiguous meaning, it does not consider any

contrary interpretations advocated by an agency, much less a so-called "clarification" that effectively overturns established Court precedent. Despite this lack of authority, the IRS has continued to assert that the Regulation interpreting the phrase "omits from gross income" to include overstatements of basis—the opposite of the conclusion reached by this Court in *Colony*—is entitled to judicial deference.

In this case, and in previous cases addressing the new regulation, the government relies in part on *Brand X* to justify deference to its new regulation. Pet'r's Br. 37; *see also*, *Carpenter Family Investments, LLC*, 136 TC No. 17 ("We think that it is reasonably clear from the preamble to the final regulations that the Secretary believes that, relying on *Brand X*, he can come to a different conclusion as to the meaning of section 6501 than the Supreme Court did in *Colony*."). The government argues that only where a judicial precedent has held that a statute unambiguously forecloses an agency's interpretation does precedent displace a conflicting agency construction. That, however, was not the holding of *Brand X*. The Court in *Brand X* concluded that the Ninth Circuit should have applied *Chevron* and deferred to the FCC's interpretation of the statute, rather than follow its own precedent, in which it had adopted a conflicting statutory construction. 545 U.S. at 1003. The Court held that "[a] court's prior judicial construction of a statute trumps an agency construction otherwise entitled to *Chevron* deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion." *Id.* at 982.

The *Brand X* Court also stated, however, that where a court has previously found a statute to be unambiguous, precedent forecloses a contrary agency construction. *Brand X*, 545 U.S. at 984 (citing *Neal v. United States*, 516 U.S. 284 (1996)). Moreover, *Brand X* did not address this Court's previous rulings and, in his *Brand X* concurrence, Justice Stevens noted that the Court's analysis "would not necessarily be applicable to a decision by this Court that would presumably remove any pre-existing ambiguity." *Brand X*, 545 U.S. at 1003. Where the instructions of Congress are considered by the Supreme Court to be unambiguous, the Treasury is not left with an interpretative or advisory role, or with the authority to issue a contrary interpretation, even when issued as a regulation. To find otherwise would be to grant to an agency more legislative power than Congress itself wields.

In his *Brand X* dissent, Justice Scalia raised a hypothetical future agency action, which unfortunately parallels the actions of the agency here. He posed a circumstance in which the agency itself was a party to the case in which the Court construes a statute, and the agency then disregards that construction and seeks *Chevron* deference for its own contrary construction the "next time around." *Id.* at 1017 (Scalia, J., dissenting). He then correctly posited that this overturning of Court precedent by agency rulemaking is "bizarre" and "probably unconstitutional." *Id.* (citing *Chicago & Southern Air Lines, Inc. v. Waterman S.S. Corp.*, 333 U.S. 103, 113 (1948) ("Judgments within the powers vested in courts by the Judiciary Article of the Constitution may not lawfully be revised, overturned or refused faith and credit by another Department of

Government.")). Justice Scalia was correct in both his prediction of the manner in which an agency would hope to apply the Court's decision in *Brand X*, and the characterization of the result.

As in Justice Scalia's *Brand X* dissent, his dissent in *United States v. Mead Corp.*, in which the Court examined the deference to be given to an agency regulation, raised another hypothetical that predicted the IRS's actions here. 533 U.S. 218, 247-48 (2001). In that hypothetical an agency readopts an interpretation of a regulation previously rejected by a court by repromulgating it through a *Chevron*-eligible procedural format—in other words, precisely what the Petitioner seeks to do here. Justice Scalia stated that approving this procedure would be "a landmark abdication of judicial power" and "worlds apart from *Chevron* proper." *Id.* (Scalia, J., dissenting). Indeed, for the Court to approve that procedure as urged by the government would both be a radical departure from the current *Chevron* framework and an abdication of judicial power that, as Justice Scalia suggested in *Brand X*, would be both bizarre and likely unconstitutional. Though both hypotheticals were raised in dissents, neither reflected the result of the actual holdings in either *Mead* or *Brand X*.

Indeed, the majority in *Brand X*, when addressing Justice Scalia's concerns, does not contemplate that its holding could be used to advance the type of abuse of authority the IRS engaged in here. *See* 545 U.S. 967, 982-84. Similarly, in *Mead*, while the majority does give deference to the agency choice, it does so under circumstances where there was a lack of indication by Congress as to whether or not it intended to

delegate rulemaking authority to the agency. 533 U.S. 218, 237. The *Mead* holding does not tread upon the dangerous idea of allowing an agency to change or promulgate rules that directly contradict Supreme Court precedent in order to put itself in a better position for litigation. The Court should not extend both precedents to reach the action taken by the IRS here.

C. DEFERENCE SHOULD NOT BE EXTENDED TO THE REGULATION UNDER *CHEVRON* STEP TWO

Even assuming the language of § 6501(e)(1)(A) is ambiguous, *Chevron*'s step two does not justify deference to the unreasonable Regulation. The second step of *Chevron* requires that, if the statute is "silent or ambiguous," the court will defer to an agency's "permissible construction of the statute." *Chevron*, 467 U.S. at 843, 104 S. Ct. 2778.

In *Mayo Foundation for Medical Education and Research v. United States*, 131 S. Ct. 704 (2011), the Court recently revisited *Chevron* in the context of an IRS Treasury Regulation, holding *Chevron* is to be applied in the tax context. There are limits to *Chevron* deference, however, even in step two. In *Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 213, 109 S. Ct. 468 (1988), the Court recognized one such limit, stating that "[d]eference to what appears to be nothing more than an agency's convenient litigating position" is "entirely inappropriate." Citing *Bowen* when analyzing the Regulation at issue here, the Fifth Circuit in *Burks v. United States*, noted that even if *Chevron* step two were applied, it was at best "unclear" whether the Regulation would be subject to *Chevron* deference, where the Treasury had during

the "pendency of litigation" promulgated "determinative, retroactive regulations following prior adverse judicial decision on the identical legal issue." 633 F.3d 347, n.9 (5th Cir. 2011) (citing *Chock Full O'Nuts Corp. v. United States*, 453 F.2d 300, 303 (2d Cir. 1971) ("The Commissioner may not take advantage of his power to promulgate retroactive regulations during the course of a litigation for the purpose of providing himself with a defense based on the presumption of validity accorded to such regulations.").

If the Regulation is retroactively applied to Home Concrete's 1999 tax return, the IRS will have successfully avoided the running of both the three-year statute of limitations applicable when the lawsuit began, and the six-year statute of limitations the IRS created during the litigation. Moreover, Home Concrete will be found liable for unpaid taxes for the 1999 tax year, the liability for which was not created by the IRS until 2009. The ability of an agency to change the laws governing ongoing litigation in which it is embroiled, and to receive judicial deference of its interpretations of those laws, will give the agency the ability to create liability tailored to each of its opponents.

Extending judicial deference and the force of law to what amounts to simple gamesmanship by a litigation opponent to secure a victory, would amount to a major departure from the framework of *Chevron* deference. Following such a decision, the IRS would exercise unprecedented discretion to legislate while litigating, after which a taxpayer finding itself facing the IRS in litigation would be subject to retroactive laws drafted by its litigation opponent and applied by the court according to the

instruction of that same opponent. That represents a breakdown in "conventional" litigation and, more broadly, a subversion of the rule of law.

CONCLUSION

This Court has consistently held that, where a statute has an unambiguous meaning, an agency's contrary interpretation is not entitled to deference.

Under the government's proposed framework, IRS officials, not the tax code, would rule taxpayers, and litigants would be unable to rely on the Court's precedent. Taxpayers would be unable to assess liability at the time it was incurred or anticipate what rules would be applied to them at a later date. The ability for an agency to legislate laws tailored to the litigation in which it is currently engaged would alter basic rule-of-law assumptions regarding the fairness and reliability of laws and their application by the courts.

For the foregoing reasons, the judgment of the court of appeals should be affirmed.

DATED: December 22, 2011.

Respectfully submitted,

Elizabeth Milito
Counsel of Record
Karen R. Harned
Katherine A. Isard
NATIONAL FEDERATION OF
INDEPENDENT BUSINESS
SMALL BUSINESS
LEGAL CENTER
1201 F Street, N.W., Suite 200
Washington, DC 20004
elizabeth.milito@nfib.org
(202) 406-4443

Counsel for Amicus Curiae
National Federation of
Independent Business Small
Business Legal Center

Ilya Shapiro
Counsel of Record
CATO INSTITUTE
1000 Mass. Ave., N.W.
Washington, D.C. 20001
(202) 842-0200
ishapiro@cato.org

Counsel for Amicus Curiae
Cato Institute

AMICUS CURIAE BRIEF

RECORD
AND
BRIEFS

No. 11-139

In The
Supreme Court of the United States

UNITED STATES OF AMERICA,

Petitioner,

v.

HOME CONCRETE & SUPPLY, LLC, ET AL.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Fourth Circuit

BRIEF OF UTAM, LTD. AND DSDBL, LTD. AS AMICI CURIAE IN SUPPORT OF RESPONDENTS

JAMES F. MARTENS
Counsel of Record
AMANDA M. TRAPHAGAN
MARTENS, SEAY & TODD
301 Congress Avenue
Suite 1950
Austin, Texas 78701
(512) 542-9898
jmartens@textaxlaw.com

Attorneys for Amici Curiae

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

Library of Congress
Law Library

TABLE OF CONTENTS

Page

INTEREST OF AMICI CURIAE 1

SUMMARY OF ARGUMENT 1

ARGUMENT 3

I. THE UNITED STATES'S ASSERTION THAT IT IS DIFFICULT TO DETECT "SON-OF-BOSS" TRANSACTIONS IS BOTH FACTUALLY WRONG AND IRRELEVANT 3

II. THE COURT SHOULD NOT AFFORD *CHEVRON* DEFERENCE TO THE NEW REGULATIONS BECAUSE THEY ADDRESS AN AREA OUTSIDE TREASURY'S EXPERTISE 9

CONCLUSION 15

APPENDIX

Notice 2000-44 Son of Boss Transaction Toolkit for Financial Products & Transaction Examiners 1a

TABLE OF AUTHORITIES

Page

CASES:

Badaracco v. Comm'r, 693 F.2d 298 (3d Cir. 1982), *aff'd*, 464 U.S. 386 (1984) 12

Bamidele v. INS, 99 F.3d 557 (3d Cir. 1996) 10, 11, 12

Branerton Corp. v. Comm'r, 61 T.C. 691 (1974) 4

Chase Securities Corp. v. Donaldson, 325 U.S. 304 (1945) 9

Chevron U.S.A., Inc. v. NRDC, 467 U.S. 837 (1984) 2, 9, 10, 11, 14

Consol. Bearings Co. v. United States, 166 F. Supp. 2d 580 (Ct. Int'l Trade 2001) 10

Dion v. Secretary of Health and Human Serv., 823 F.2d 669 (1st Cir. 1987) 10

Garcia v. Attorney General, 553 F.3d 724 (3d Cir. 2009) 10

Home Concrete & Supply LLC v. Comm'r, 634 F.3d 249 (4th Cir. 2011) 13, 14

Murphy Exploration and Production Co. v. U.S. Dept. of the Interior, 252 F.3d 473 (D.C. Cir. 2001) 10

Oliver M. Elam, Jr. v. Baldridge, 771 F.2d 174 (6th Cir. 1985) 10

Pension Ben. Guar. Corp. v. LTV Corp., 496 U.S. 633 (1990) 10

TABLE OF AUTHORITIES – Continued

Page

Talk Am., Inc. v. Michigan Bell Tel. Co., 131 S.Ct. 2254 (2011) 13

The Colony, Inc. v. Comm'r, 257 U.S. 28 (1958) 12

STATUTES:

26 U.S.C. § 6011(a) 7

26 U.S.C. § 6501(e)(1)(A) 11, 12, 14

26 U.S.C. § 6707A(c)(2) 8

26 U.S.C. § 7602 8

RULES AND REGULATIONS:

Supreme Court Rule 37 1

26 C.F.R. § 1.6011-4(b)(2) 8

26 C.F.R. § 301.6229(c)(2)-1 2

26 C.F.R. § 301.6501(e)-1 2

T.D. 8877, 2000-1 C.B. 727 8

T.D. 9000, 2002-2 C.B. 87 8

OTHER AUTHORITIES:

Notice 2000-44, 2000-2 C.B. 255 ..... 4, 7

Notice 2000-44 Son of Boss Transaction Toolkit for Financial Products & Transaction Examiners 4, 6, 9

Statement of Senator Ashurst, 67 Cong. Rec. 3481, 3852 (1926) 12

INTEREST OF AMICI CURIAE

Pursuant to Supreme Court Rule 37, UTAM, Ltd. and DSDBL, Ltd. ("Amici" hereinafter) submit this brief as amici curiae in support of respondents.[1]

Amici are two related entities that are currently litigating cases that present the overlapping issues before the Court here. Petitions for certiorari are pending before this Court in both cases. *Comm'r v. DSDBL, Ltd., et al.*, No. 11-581; *UTAM, Ltd., et al. v. Comm'r*, No. 11-747. The Court's ruling here may control the disposition of these petitions on the issues presented here.[2] Therefore, the Amici provide additional facts and legal analyses to assist the Court.

SUMMARY OF ARGUMENT

The Amici urge this Court to find in Home Concrete's favor for the reasons set forth in Home

[1] Pursuant to Supreme Court Rule 37.6, counsel for Amici certifies that no counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person or entity other than Amici and their counsel contributed monetarily to the preparation and submission of this brief. The parties have filed blanket consent for the submission of amicus briefs.

[2] UTAM Ltd.'s petition also presents the issue of whether a late-filed partnership notice suspends the running of an individual's statute of limitations when the IRS fails to issue a notice of deficiency to the individual.

Concrete's brief. In addition, the Amici provide two additional arguments supporting Home Concrete's position.

First, the Court should reject the United States's assertions that it is "extremely difficult" for the IRS to detect Son-of-BOSS transactions. This assertion is factually wrong. The IRS had the tools and resources it needed to identify these transactions within the three-year limitations period. The IRS was well aware of the nature of these transactions at least as early as mid-2000, and likely even earlier. It developed and published a comprehensive audit program tailored specifically to Son-of-BOSS transactions which informed its auditors of the nine factors appearing on the face of federal income tax returns that provided clues of Son-of-BOSS transactions. Further, the United States does not dispute that Home Concrete and the other parties appearing before the circuit courts on these issues fully complied with the reporting requirements mandated by the IRS and in effect at the time the transactions were reported on the affected federal income tax returns.

Second, the Court should not defer to the new regulations (26 C.F.R. §§ 301.6229(c)(2)-1, 301.6501(e)-1) under *Chevron U.S.A., Inc. v. NRDC*, 467 U.S. 837 (1984) (*"Chevron"*) because they concern an area outside of the Treasury's expertise. Interpreting a statute of limitations is a legal issue within the expertise of courts, not executive agencies. As a result, courts have declined to apply *Chevron* deference to agency interpretations of statutes of limitations.

Further, allowing Treasury to interpret this statute of limitations would undermine its fundamental purposes of encouraging parties to act diligently and providing repose. This is because the Treasury focuses instead on applying an income definition which was written for reasons unrelated to the statute of limitations in issue. It does this in order to excuse its own delays and keep alive disputes about transactions that occurred over a decade ago. The statute of limitations is, by its nature, a Congressional limit or check on Treasury's power. Our tri-partite system of government provides legislative limits on the executive's ability to reach back in time and make adverse assessments. Therefore, the Court should not defer to the new regulations.

ARGUMENT

I. THE UNITED STATES'S ASSERTION THAT IT IS DIFFICULT TO DETECT "SON-OF-BOSS" TRANSACTIONS IS BOTH FACTUALLY WRONG AND IRRELEVANT.

The United States asserts that it is appropriate to apply the extended statute of limitations to Home Concrete and others because the transactions are "extremely difficult" to detect. For instance, on page 5 of its brief, the United States says that, in 2004, "it was critically important whether the IRS had three or six years from the filing of their returns to assess additional income taxes, because their treatment of the two parts of a Son-of-BOSS shelter . . . made it

extremely difficult for the IRS to discern that the taxpayers were in fact executing the Son-of-BOSS avoidance scheme."

This statement is factually wrong. The IRS first publicly identified the Son-of-BOSS transaction in Notice 2000-44, 2000-2 C.B. 255, which it issued on August 11, 2000. The IRS also developed a detailed framework for identifying Son-of-BOSS transactions. It formally published this framework in a document entitled "Notice 2000-44 Son of Boss Transaction Toolkit for Financial Products & Transaction Examiners" ("Son-of-BOSS Toolkit"). We attach a copy of the Son-of-BOSS Toolkit as an appendix to this brief.[3]

The Son-of-BOSS Toolkit brings together several IRS documents discussing Son-of-BOSS transactions. It provides auditors with numerous tools for identifying returns reporting Son-of-BOSS transactions. It lists nine ways to identify the affected tax returns. All nine relate to items reported on the face of the affected returns. None of them relate to items left off of the returns. They are (verbatim):

---

[3] The Commissioner of Internal Revenue provided the Son-of-BOSS toolkit (version March 26, 2003) to the Amici's counsel on October 15, 2007 in response to discovery requests the Amici made under the procedures set forth in *Branerton Corp. v. Comm'r*, 61 T.C. 691 (1974). The Amici each included copies of the Son-of-BOSS Toolkit with the motions for summary judgment they filed in the Tax Court. The Appendix filed in UTAM, Ltd.'s case before the D.C. Circuit Court of Appeals also contained the Son-of-BOSS Toolkit at pages 287-310.

1. Look for large losses (either capital or ordinary). The ordinary losses generally involve exchanges of foreign currencies under § 988;

2. Look for pass-through entities beginning and ending within the same tax year;

3. Be alert for other entities of a pass-through nature. For example, single member LLC (disregarded entity), multi-member LLC electing partnership status, partnerships with one partner holding a high percentage (greater than 90%) and a related party holding a minor percentage (less than 5%), Subchapter S corporation owned by TP, and grantor trusts;

4. Look for large attorney, accounting and/or consulting fees;

5. Look for contributions in exchange for partnership interests and subsequent assignment or redemption of partnership interest within a short time causing a technical termination of the partnership;

6. Look for use of financial products such as short sales, options, straddles, foreign currencies and/or other derivatives as part of the contribution in exchange for partnership interests and/or redemptions of partnership interests;

7. Look for situations that utilize apparently "unrelated" pass-through type entities at any step within the scheme;

8. Be alert to netting of income and losses. Review Schedule M-1 for indications of tax losses not on the book that suggest that the losses are netted amounts on the tax returns; and

9. Review Schedule M-2 of Form 1065. Especially be aware of large capital contributions on line 2. TPs report the cash proceeds of short sales, but disregard the open position liability.

The Son-of-BOSS Toolkit describes three different types of Son-of-BOSS transactions and provides schematic illustrations of each. It lists the taxpayer documents an auditor should request if the auditor suspects a Son-of-BOSS transaction and provides an exhaustive list of audit questions to ask taxpayers. Thus, far from finding it "extremely difficult" to detect Son-of-BOSS transactions, the IRS was able to publish guidance for its examiners setting forth guidelines for identifying such transactions *all based on information provided on the face of a return*.

Further, while the United States claims that Home Concrete and others concealed these transactions, it alleges no violations of any of the reporting rules it promulgated for the affected years. Home Concrete and others appearing before the circuit courts fully complied with all of the reporting and disclosure requirements then in effect.[4] They properly

[4] The Amici filed uncontroverted expert reports by Jerry L. Hamilton, CPA, with their Motions for Summary Judgment

(Continued on following page)

and accurately reported the transactions in issue in light of their legal positions. Here, as in other cases, those legal positions were supported by the written opinions of then-prominent, well-respected law firms.

The Internal Revenue Code requires taxpayers to file their returns "according to the forms and regulations prescribed by the Secretary" and to include "the information required by such forms and regulations." 26 U.S.C. § 6011(a). In none of these cases has the United States identified any statute, regulation, form, or instruction that required disclosures that were not made. Moreover, the IRS has never alleged that Home Concrete or the others appearing before the circuit courts engaged in any conduct that triggered the fraud exception to the ordinary limitations period.

The IRS knew, at least as early as 2000, that taxpayers had engaged in these transactions, but chose not to change its reporting requirements until 2002. In 2000, the IRS released Notice 2000-44, which identified the Son-of-BOSS transactions and characterized them as "listed transactions."[5] At that

---

before the Tax Court stating that a reasonable revenue agent would have selected their returns for audit. The joint appendix filed in UTAM Ltd.'s case before the D.C. Circuit Court of Appeals also contains this report at p. 311-355. Mr. Hamilton is a former IRS revenue agent who managed IRS return examiners tasked with choosing returns for examination.

[5] Listed transactions are transactions that are the same as or substantially similar to transactions the IRS has identified as tax avoidance transactions by notice, regulation, or other form of

(Continued on following page)

time, the IRS's regulations required only C Corporations to make additional disclosures for the listed transactions. *See* T.D. 8877, 2000-1 C.B. 727. Even though the IRS knew that Son-of-BOSS transactions involved partnerships and other flow-through entities, it delayed until June 2002 to impose additional reporting requirements. *See* T.D. 9000, 2002-2 C.B. 87.

The IRS had another tool at its disposal. It had the authority under 26 U.S.C. § 7602 to issue summonses to alleged promoters of Son-of-BOSS transactions. However, the IRS delayed its issuance of these summonses and then delayed acting upon the information it received. Here, the IRS waited until June 19, 2003 – *after* the expiration of the three-year limitations period for Home Concrete's 1999 return – to issue a summons to Jenkens & Gilchrist. Pet. at 26a-27a. Even though Jenkens & Gilchrist identified the Home Concrete taxpayers to the IRS as having engaged in a Son-of-BOSS transaction on May 17, 2004, the IRS did not begin its audit of their returns until January 25, 2006, almost six years after the return was filed. Joint Appendix at 30.

---

published guidance. 26 U.S.C. § 6707A(c)(2); 26 C.F.R. § 1.6011-4(b)(2). The IRS regularly reviews these transactions and sometimes removes them from its list of listed transactions. *See* Internal Revenue Service, "Listed Transactions – LB&I Tier I Issues" *available at* http://www.irs.gov/businesses/corporations/article/0,,id=120633,00.html.

The IRS had the resources and knowledge it needed to identify returns reporting these transactions within the three-year limitations period. It had the Son-of-BOSS Toolkit. It had the taxpayers' returns. It had summons authority. It is only the IRS's delays and choices that kept it from acting within the three-year limitations period. This Court should not allow the United States to re-interpret the application of the extended limitations period in order to dig itself out of the hole it created.

Finally, the United States's assertions regarding the underlying nature of the transactions at issue and its claim that it is "extremely difficult" to detect Son-of-BOSS transactions are irrelevant to determining whether the requisite gross income was omitted. As this Court has recognized, statutes of limitations are "by definition arbitrary, and their operation does not discriminate between the just and unjust claim, or the voidable and unavoidable delay." *Chase Securities Corp. v. Donaldson*, 325 U.S. 304, 314 (1945).

II. THE COURT SHOULD NOT AFFORD *CHEVRON* DEFERENCE TO THE NEW REGULATIONS BECAUSE THEY ADDRESS AN AREA OUTSIDE TREASURY'S EXPERTISE.

The Court should not defer to the new regulations under *Chevron U.S.A., Inc. v. NRDC*, 467 U.S. 837 (1984) ("*Chevron*"), because the new regulations interpret a statute of limitations, which is outside

Treasury's expertise. As this Court has recognized, the crux of *Chevron* deference is "practical agency expertise." *Pension Ben. Guar. Corp. v. LTV Corp.*, 496 U.S. 633, 651 (1990). "The deference due an agency's interpretation depends, in the first instance, on whether the matter is more properly viewed as within the agency's expertise or, on the contrary, as a clearly legal issue that courts are better equipped to handle." *Dion v. Secretary of Health and Human Serv.*, 823 F.2d 669, 673 (1st Cir. 1987). Accordingly, "[a]bsent congressional delegation, if an agency has promulgated a regulation outside the scope of its specialized knowledge, courts will not defer to it." *Murphy Exploration and Production Co. v. U.S. Dept. of the Interior*, 252 F.3d 473, 479 (D.C. Cir. 2001); *see also Oliver M. Elam, Jr. v. Baldridge*, 771 F.2d 174 (6th Cir. 1985) (observing that "[w]hen interpretation of the statute does not require special knowledge within the agency's field of technical expertise, reviewing courts sometimes accord little deference to the agency's construction.").

Interpreting a statute of limitations presents a legal question within the expertise of courts, not that of executive agencies. As a result, courts have declined to apply *Chevron* deference to agency interpretations of statutes of limitations. *See, e.g., Garcia v. Attorney General*, 553 F.3d 724, 727 (3d Cir. 2009); *Consol. Bearings Co. v. United States*, 166 F. Supp. 2d 580, 583-84 (Ct. Int'l Trade 2001). *Bamidele v. INS*, 99 F.3d 557, 561 (3d Cir. 1996) ("*Bamidele*") is instructive.

Bamidele involved the INS's interpretation of the statutes of limitations for deportation and for rescission of adjustment of immigration status. 99 F.3d at 558. The relevant statute stated that the statute of limitations for rescission of adjustment of immigration status was five years, but provided no separate statute of limitations for deportation. *Id.* at 562-563. The INS initiated deportation proceedings against Bamidele six years after it adjusted his immigration status to permanent resident. *Id.* at 559. Bamidele argued that the statute of limitations for rescission of adjustment of immigration status barred the INS's deportation order because the law required the INS to adjust his status before deporting him. *Id.* at 560. However, under the INS's interpretation of the statutes, the statute of limitations did not bar the deportation order because no separate statute of limitations existed for deportation. *Id.*

The *Bamidele* court disagreed. It refused to afford *Chevron* deference to the INS's interpretation of the statute of limitations for deportation, reasoning that "[a] statute of limitations is not a matter within the particular expertise of the INS." *Id.* at 561. Instead, the court found that the interpretation of a statute of limitations is "a clearly legal issue that courts are better equipped to handle." *Id.* Accordingly, the court refused to defer to the INS's interpretation of the statute of limitations and found that the deportation order was time-barred. *Id.* at 565.

Similarly, this Court should not afford *Chevron* deference to Treasury's interpretation of 26 U.S.C.

§ 6501(e)(1)(A)'s limitations period. Treasury has no more expertise in interpreting statutes of limitations than the INS, so there is no reason to treat Treasury differently than the *Bamidele* court treated the INS. Even more to the point, Treasury has no more expertise in interpreting statutes of limitations than this Court. Indeed, it has far less. Interpreting statutes of limitations requires no specialized tax knowledge. In particular, interpreting the statute of limitations here requires only knowledge of the meaning of the word "omits," which this Court already clearly defined in this context in *The Colony, Inc. v. Comm'r*, 257 U.S. 28 (1958) ("*Colony*").

Allowing Treasury to interpret this statute of limitations undermines its purpose. Congress created 26 U.S.C. § 6501's statute of limitations to give taxpayers "repose." *See, e.g., Badaracco v. Comm'r*, 693 F.2d 298, 301 (3d Cir. 1982), *aff'd*, 464 U.S. 386 (1984). One of the senators who enacted the first statute of limitations on income tax assessments described its purpose as follows: "[t]he citizens of the country when they pay are entitled to a statute of repose beyond which even the governmental hand cannot reach to disturb them." Statement of Senator Ashurst, 67 Cong. Rec. 3481, 3852 (1926).

Thus, the statute of limitations is, by its nature, a Congressional limit on Treasury's power. It is dangerous to allow the Treasury to define the limits of its own power under the guise of agency expertise. Such power should remain in the hands of Congress

and the judiciary in order for statutes of limitations to have any meaning or certainty. Allowing agencies to police the limits of their own power simply encourages self-serving agency interpretations. *Cf. Talk Am., Inc. v. Michigan Bell Tel. Co.*, 131 S.Ct. 2254, 2266 (2011) (Scalia, J., concurring) (questioning *Auer* deference to an agency's interpretation of its own rules on similar grounds).

The new regulations demonstrate this. They contradict the plain language of the statute and this Court's precedent, and, here, they serve to excuse the IRS's own dilatory actions. As Judge Wilkinson recognized in his *Home Concrete* concurrence, the new regulations "pass the point where the beneficial application of agency expertise gives way to a lack of accountability and a risk of arbitrariness." *Home Concrete & Supply LLC v. Comm'r*, 634 F.3d 249, 259 (4th Cir. 2011) ("*Home Concrete*").

The new regulations purport to clarify the definition of "gross income," but do no such thing. They instead distort the meaning of the phrase "omission from gross income" in a manner that conflicts with Congress's intent in enacting the extended statute of limitations provision. To do this, the regulations apply a technical definition of "gross income," written for purposes unrelated to the statute of limitations, that Congress never referenced or otherwise expressed any intent to incorporate into the statute of limitations provisions. They also redefine the word

"omits" to mean "mathematically reduces," despite the plain meaning of the word "omits."

The regulations' conclusion subverts the natural meanings of words and directly contradicts Congress's unambiguous intent in enacting 26 U.S.C. § 6501(e)(1)(A) and this Court's precedent in *Colony*. As Judge Wilkinson noted in his *Home Concrete* concurrence, the new regulations contradict "the plain instructions of Congress, which have not been changed, and the plain words of the Court, which have not been retracted." 634 F.3d at 259. Such regulations cannot be a proper exercise of agency expertise. They appear to usurp legislative and judicial power under the guise of agency expertise. As a result, this Court should afford them no deference.

CONCLUSION

The United States' assertion that it required additional time to detect Son-of-BOSS transactions is irrelevant, but factually wrong nevertheless. Moreover, this Court should not afford *Chevron* deference to the new regulations because they purport to interpret an area outside Treasury's expertise. Therefore, for the reasons set forth in this brief

and Home Concrete's brief, the Court should find in favor of Home Concrete.

Respectfully submitted,

JAMES F. MARTENS
Counsel of Record
AMANDA M. TRAPHAGAN
MARTENS, SEAY & TODD
301 Congress Avenue
Suite 1950
Austin, Texas 78701
(512) 542-9898
jmartens@textaxlaw.com

Attorneys for Amici Curiae

Notice 2000-44

Son of Boss Transaction Toolkit

For

Financial Products & Transaction Examiners

Assembled by Donna Hovis, Carlos Bastidas, and Ronald Grote

[2] Index

Description of Transactions Encountered in the Field	3
Identification of SOB Type Transactions	3
I think I have a SOB Transaction, what do I do?	4
Three Scenarios	4
Additional Materials Provided	6
SOB Questionnaire	7
Digital Option Transaction	8
IDR for Digital Option	9
Digital Option Investor Questions	11
Digital Option Promoter Questions	16
LMSB & SB/SE Tracking Codes; UIL Codes	20
IRS Position	20
Notice 2000-44	22

[3] Description of Transactions Encountered in the Field

This collection of information is being provided to Financial Products & Transactions Specialists to assist

in recognizing and developing cases involving the Son of Boss (SOB) transaction. The materials supplied were developed through case experience.

The type of transaction (or series of transactions) referred to as the "Son of Boss" (SOB) transaction is a "listed transaction" outlined in **Notice 2000-44**, 2000-2 CB 255 (August 11, 2000). It generally refers to certain transactions that are marketed to generate tax losses through the Taxpayer's purported creation of artificially high basis in partnership interests. The Taxpayer then attempts to recognize deductible losses on the disposition of the partnership interest or assets coming out of the partnership, even though no economic loss is incurred.

In addition to the scenarios presented in **Notice 2000-44**, the Service has uncovered other variations on the same theme. There are some cases that are identifiable by their association with a particular promoter. In other cases, identification of the scheme is often difficult because the Taxpayers and promoters use a variety of entities (sometimes new, sometimes already existing) and various financial products. In addition, the losses have been reported on differing levels of tax returns and in differing locations within the tax returns. For example, foreign currency exchange losses have been shown as reductions of gross sales, cost of goods sold, other income, and other deductions, to name a few. Capital losses generally appear on the Schedule D or Form 4797. It is not at all uncommon for the losses to be netted against

other items therefore making the transaction more difficult to spot.

While the generalities of the Son of BOSS transaction are similar from case to case, the facts and the financial products used are not the same and may require different arguments or development. Therefore, it is important to develop the facts of each case.

Identification of Son of BOSS Type of Transactions

1. Look for large losses (either capital or ordinary). The ordinary losses generally involve exchanges of foreign currencies under §988;

2. Look for pass-through entities beginning and ending within the same tax year;

3. Be alert for other entities of a pass-through nature. For example, single member LLC (disregarded entity), multi-member LLC electing partnership status, partnerships with one partner holding a high percentage (greater than 90%) and a related party holding a minor percentage (less than 5%), Subchapter S corporation owned by TP, and grantor trusts;

4. Look for large attorney, accounting and/or consulting fees;

5. Look for contributions in exchange for partnership interests and subsequent assignment or redemption of partnership interest within a short time causing a technical termination of the partnership;

6. Look for use of financial products such as short sales, options, straddles, foreign currencies and/or other derivatives as part of the contribution in exchange for partnership interests and/or redemptions of partnership interests;

[4]

7. Look for situations that utilize apparently "unrelated" pass-through type entities at any step within the scheme;

8. Be alert to netting of income and losses. Review Schedule M-1 for indications of tax losses not on the book that suggest that the losses are netted amounts on the tax returns; and

9. Review Schedule M-2 of Form 1065. Especially be aware of large capital contributions on line 2. TPs report the cash proceeds of short sales, but disregard the open position liability.

I think I have a SOB transaction, what do I do?

1. If not already issued, issue the mandatory tax shelter IDR;

2. Request copies of all related returns (TEFRA may apply to pass-through returns, including single-member LLC);

3. Request LLC organization, operation, and liquidation/cancellation documents;

4. Request Partnership organization, operation, assignment, and dissolution documents;

5. Request SOB transaction documents – promotional material, schematics, minutes and notes, timeline, consulting agreements, engagement letters, opinion letters, confidentiality agreements, etc.

6. Request copies of invoices for accounting, legal, and consulting services;

7. Request computations of gain/loss and computations of basis;

8. Request copies of brokerage information – account application, trading authorization, loan agreement, margin agreement, monthly statements; confirmation statements, etc.

9. Interview taxpayer for business purpose, overall understanding of the transactions, investment/business background and expertise, etc.;

10. Inspect prior year and subsequent year returns for additional SOB transactions or evidence of additional tax shelter activity; and

11. Assure that proper codes are entered into ERCS/CEMIS (see page 20).

12. Additional Financial Products assistance: Carlos Bastidas (561-616-2095), Donna Hovis (239-936-3076), or Ronald Grote (813-315-2356).

13. Financial Products Territory Manager in charge of SOB, Robert Thorn (317-226-6070);

14. Coordinate with either of the Partnership and Pass-Through Issue Specialists – Rod Oakes, LMSB (763-549-1020 x 326) or Mike Whalin, SB/SE (763-549-1020 x 331) who are coordinating the SOB transaction.

15. Coordinate as necessary with Chief Counsel.

16. SOB Champions – Robert Brazzil, LMSB and Peggy Rule, SB/SE (See Memo available on OTSA Tax Shelter website under Issue Champions.)

Three Scenarios

The following discussion outlines three SOB scenarios encountered in the field. Each of the scenarios is further supplemented by a schematic to help visualize the money and loss flows. Although not limited to individuals, these transactions have been identified on tax returns related to high income individuals and tax returns where a large capital gain was generated, for example from the sale of a business. It is also important to note that the transaction starts [5] in one entity, the loss is shown on another entity, and the ultimate effect of the loss appears on another entity. The following may help in identifying potential SOB transactions.

Scenario 1 – Short Sale of Treasury Notes

Taxpayer forms a single member LLC and funds it with cash. Shortly thereafter, the LLC opens a brokerage account at Big Brokerage. On date 1, the LLC

sells $XX million Treasury Notes short and receives proceeds in its Brokerage account. Also on Date 1, the LLC and A Corp. (Sub S owned by TP's grantor trust) form XYZ Partnership. LLC contributes the short sale proceeds, the open short position, and additional margin cash in exchange for 99% interest in XYZ partnership. A Corp. contributes margin cash in exchange for 1% interest in the partnership. LLC claims their outside basis in the partnership is $XX million proceeds + margin cash.

On Date 2, XYZ Partnership covers the open short position by buying $XX million in Treasury Notes and recognizes a small economic gain or loss. A few days or weeks later, Date 3, XYZ buys either stock or foreign currencies using the original margin cash. On Date 4, LLC assigns its interest in XYZ Partnership to A Corp. causing a technical termination. XYZ Partnership assets, stock or foreign currencies, are liquidated into A Corp. LLC's outside basis ($XX million + cost of stock or currency) is assigned to the assets transferred to A Corp. Before year end, Date 5, A Corp. sells off all or portions of stock or foreign currency and claims either capital loss or ordinary loss essentially equivalent to the original short sale proceeds. Since A Corp. is a Sub-chapter S company, the loss is passed through to the TP's grantor trust and on to the TP's Form 1040.

See, SOB Scenario Charts.xls; T-Note Chart

Scenario 2 – Options through an Intermediary

TP, through a single member LLC (disregarded for tax purposes), opens an account with Grand Advisor by depositing cash. On Date 1, Grand Advisor in the name of LLC buys 3 currency options for $12 million premiums and simultaneously sells 3 currency options and receives premiums of $11.8 million (net out-of-pocket $200,000). A short time later, on Date 2, the 6 options (FMV $ 45,000) and cash are contributed to Fund LLC in exchange for an interest in Fund LLC. Fund LLC elects to be treated as a partnership under the check-the-box regime. LLC claims their outside basis for the interest in Fund LLC is $12 million paid in premiums for options purchased.

Under the Fund LLC Subscription Agreement, members may request redemption of their interest upon 30 days notice. Within the first 30 days, the LLC requests its interest be redeemed by Fund LLC. On Date 3, Fund LLC distributes foreign currency and cash to LLC in redemption of its interest. Since the LLC is treated as a partnership, the withdrawal of a member (partner) causes a technical termination. Therefore, the foreign currency distributed to LLC has a basis equal to the outside basis of LLC (alleged to be $12 million). Immediately after the distribution, the foreign currency is exchanged for US Dollars. Ordinary loss is recognized on the exchange under §988 and deducted on the TP's tax return.

[6] See, SOB Scenario Charts.xls; Options – Intermediary Chart

Scenario 3 – Digital Options

TP, through a single member LLC, sells a short option in foreign currency for which a premium is received. Simultaneously, the LLC buys a long option in foreign currency and pays a premium. The strike prices of the options differ by .002. On Date 2, the options and cash are transferred to a newly formed partnership, ABC, in exchange for a majority interest in the ABC Partnership. After 30 days, the options will expire either in the money or out of the money. The partnership recognizes the economic gain or loss on the spread. Depending on the type of loss desired, the partnership will either invest in foreign currency or capital stock.

On Date 4, the LLC will transfer its interest in ABC Partnership to a newly formed S-Corp. This transfer causes a technical termination that, in turn, causes the partnership assets (foreign currency or stock) to be distributed to the S-Corp. Before year-end, the S-Corp sells the assets received from the partnership and recognizes a loss for tax purposes that is passed through to the TP as owner of the S-Corp.

See, SOB Scenario Charts.xls; Digital Option Chart

Additional Materials Provided

The following files are provided to assist you in gathering the information needed to develop your case and in analyzing the transactions.

Excel Files:

- SOB Questionnaire Template (below and attached excel file)
- Schematics – SOB Scenario Charts.xls.
- Documents to request – SOB Document Inventory.xls
  - T-Note Short Sale Inventory (tab)
  - Digital Option Inventory (tab)
- SOB-Short Sale Trf. of Funds Broker Accts.xls
- SOB-Analysis of Options.xls
- SOB-Cash Flow Analysis of Digital Options.xls
- SOB-Tax-Book Digital Option Analysis

Word Documents:

- IDR Digital Options
- Digital Option Investor Questions.doc
- Digital Option Promoter Questions.doc

PowerPoint:

- SOB PowerPoint
- BofB PowerPoint

[7] Son of BOSS Questionnaire

Use the following questions to help identify potential Son of BOSS types of transactions and cases. Refer to Notice 2000-44, 2000-2 CB 255 (August 11, 2000). If you answer the majority of the questions "Yes," it is likely you have a SOB type of case. It is highly encouraged that you compare your known facts with SOB Scenarios 1-3. SOB cases have arisen

on high income individuals, with and without other businesses (e.g., partnerships & 1120-S corps.), and in cases where large capital gains have been generated (e.g. sales of business). The initial transaction occurs in one entity and then is passed to a second entity (e.g. a partnership). Inflated basis is passed to a third entity through a technical termination where the loss is typically incurred. The ultimate tax effect of the loss may then be passed on due to the pass through nature of the entity reporting the loss transaction. If you believe you have a SOB case, refer the case to LMSB Financial Products and Transactions for assistance in evaluating the financial products utilized and further developing the case. See LMSB, Financial Products & Transactions website for referral procedures and forms.

This questionnaire was developed from case experiences. However, use of different financial products and factual twists may be included in your case. **Although your case may not fit exactly in the fact patterns presented, it may still fit under Notice 2000-44. In addition, there are other listed transactions containing similar elements that may be identified in answering these questions. In situations where you are uncertain that your case is a SOB case, it is better to refer the case to Financial Products and Transactions for evaluation than to do nothing.**

TAXPAYER:
YEAR(S):

SON OF BOSS QUESTIONS	YES	NO
Is there a disclosure under Announcement 2002-02?		
Does the TP typically have high amounts of ordinary income?		
Did TP income rise substantially recently or in this year?		
Is TP income uncharacteristically low or off-set by losses (including losses from pass-through)?		
Has the TP sold or exchanged a business or other assets for a large capital gain?		
Are large capital losses reported?		
Are there losses from the sale or exchange of foreign currencies under Sec. 988?		
Is income from pass-through entities off-set by losses from other pass-through entities?		
Is there evidence of assignment of partnership interests?		
Is there evidence of short sales?		
Is there evidence of buying or selling derivatives?		
Based on the asset involved, is there a large disparity between sales price and basis?		
Is there evidence of large or unusual fees to attorneys, accountants, consultants, or others?		
Did the TP organize a limited liability company? Single member LLCs are disregarded entities.		
Did the TP form a partnership that terminated by year-end?		
Did the TP form a corporation and elect Subchapter S status?		
Did the TP form a grantor trust?		

Was the tax return(s) prepared by a firm other than the firm usually preparing the return(s)?	
Is there evidence of a new brokerage firm being used by the TP?	
Does there appear to be short-lived investments in "unrelated" entities or brokerages?	
What is the stated business purpose for each of the entities formed?	
Is there evidence or indication of netting?	
Does Schedule M-1 indicate gains or losses not directly traceable to a return line item?	
Are there any indications of any of the elements shown in SOB Scenarios 1-3?	
Factual Comments and Notes	

[8] **Digital Option Transactions**

There are several versions of the Notice 2000-44 transactions. One of the variants described in the Notice includes a transaction involving the purchase and simultaneous sale of foreign currency digital (binary) options with slightly different strike prices.

Digital Options

Essentially, a digital option is one of several types of "exotic options." Unlike a standard, plain vanilla option, in which the payoff depends on the underlying asset, digital options pay either a fixed amount or nothing, depending only on whether the spot price is above or below the strike.

For example, the partnership entered into the following digital option positions simultaneously:

Long Call EUR/JPY Strike 103.95
payout EUR 42,000,000 premium EUR 12,600,000

Short Call EUR/JPY Strike 103.96
payout EUR 41,877,000 premium EUR 12,538,531

Depending on the terms of the contract and the movement of the spot rate in relation to the strike price, the partnership will either net nothing or net the difference between the long payout and short payout amounts. It does not matter how far the spot price moves from the strike price only that it moves. The payout is not determined by the degree of movement, rather it is limited to the amount stated in the contract. In this case, the terms of the long contract state that Seller (counterparty) will pay buyer (partnership) if the spot rate at expiration is equal to or greater than the strike price. If, for example, the spot rate is 104.85, then the counterparty must pay the partnership EUR 42,000,000. The terms of the short contract state that Seller (partnership) will pay buyer (counterparty) if the spot rate at expiration is equal to or greater than the strike price. If, for example, the spot rate is 104.85, then the partnership must pay the counterparty EUR 41,877,000. The result of the spot rate moving up from the strike prices is a net payout received by the partnership of EUR 123,000. However, if the spot rate in this case is 103.85, nothing is paid out be either party.

In all the cases we have seen, the net premium exchanged is actually the fee that is owed to the counterparty [bank/brokerage] for entering into the transactions.

The digital option transactions operate as follows:

Step One: The partnership purchased an over-the-counter, cash-settled, European-style digital call option in a foreign currency and simultaneously sold an over-the-counter, cash-settled, European-style digital call option in the same foreign currency. The strike prices vary by .001. We believe this variance is the fee due the counterparty. The counterparty is REFCO, Bermuda. The maturity date on the contracts is four months later.

Step Two: Several days after the option transactions were entered into, the partnership assigned both open positions to an LLC in exchange for a member interest. The business objective of the LLC was to accomplish capital appreciation. The partnership took the position [9] that its basis in the LLC was increased by the cost of the purchased option but was not reduced by the sold option. Therefore, the assignment of the options to the LLC created an artificial basis for the partnership.

Step Three: Approximately thirty days before the option contracts were set to expire, the partnership entered into a Loan Agreement with Foreign Broker. The terms of the agreement provided for a term of

five years with semi-annual interest at six month LIBOR plus ten basis points. The loan was secured by a pledge of the funds in the partnerships' trading account to which the funds were deposited as well as a pledge of the Limited Partner's interest in the partnership. It appears that this "loan" was needed to increase basis for the partnership since the losses reported on the return were greater than the basis created by the long position itself.

Step Four: Several days before the option contracts were set to expire, the partnership requested liquidation of its interest in the LLC. Pursuant to the terms of the LLC agreement, the partnership was paid an amount in foreign currency that approximated its basis in the partnership. The foreign currency distribution was treated as a distribution of property and the partnership did not recognize gain or loss upon receipt. As a result, the partnership's basis in the foreign currency was equal to the partnership's basis in its interest in the LLC.

Step Five: The partnership sold the foreign currency to a third party for market value. The sale of the foreign currency resulted in a section 988 ordinary loss.

Digital Options IDR:

Please provide the following:

1. Complete copies of the [**Insert Year**] Federal tax returns of [**Insert Partnership Name**] [**Insert LLC Name**] [**Insert S-Corporation**

Name] [Insert Trust Name] [Insert 1040 Name(s)].

2. Copies of all Forms 8264 – Tax Shelter Registration – filed.

3. Copies of all disclosures made on any return or under Internal Revenue Service Announcement 2002-02.

4. Copies all documents and other materials, including legal opinions and memoranda, provided by any party that promoted, solicited, or recommended participation in the currency option transaction.

5. Copies of all legal, accounting, financial, and economic opinions and memoranda prepared for you or on your behalf in connection with the currency option transaction.

6. Copies of all correspondence, memorandum, presentations, flowcharts, models, or emails pertaining to the currency option transaction that were either given to you or [10] prepared by you for purposes of making your decision to enter into the currency option transaction.

7. A description of the tax treatment of the currency option transaction, including tax benefits claimed on the returns. In describing the tax treatment, include all tax rules or mechanics that affect, give rise to, or result in the claimed tax benefits.

8. A list of all participants and their role in the transaction.

9. The names and addresses of all parties who promoted, solicited, or recommended your participation in the currency option transaction and to whom you paid fees or other compensations in connection with your decision to participate in the currency option transaction.

10. Copies of cancelled checks, wire transfers and/or other substantiation for all fees paid or other compensation paid to all parties in connection with the currency option transaction.

11. Copies of any and all agreements entered into with respect to the currency option transaction, including, but not limited to:

    a. Partnership Agreements;
    b. Trust Agreements;
    c. Articles of Incorporation;
    d. Management Agreements;
    e. Asset Allocation Agreements;
    f. Trading Advisory Agreements;
    g. Loan Agreements;
    h. Deposit Agreements;
    i. Collateral Agreements;
    j. Master Foreign Exchange Agreements;
    k. Assignment Agreements.

12. Copies of all trade tickets, confirmations, or other similar evidence of transactions carried out through the brokerage accounts including all documents related to the digital foreign currency option transactions and all foreign currency purchase and sales transactions.

13. Copies of all brokerage statements related to the currency option transaction for the years [**Insert Year(s)**] on all accounts of the individual investor(s) and all the related entities; including but not limited to:

    a. New Account Applications;
    b. Monthly Statements;
    c. Ancillary Statements;
    d. Transactional Invoices or Receipts.

[11]

14. Copies of the cancelled checks, wire transfers, and/or any other substantiation for funding the brokerage accounts.

15. If payments were made on any loans obtained by the individual investor(s) or by any of the entities, specify the date and amount of principal and interest for each payment made.

16. Copies of the cancelled checks, wire transfers, and/or any other substantiation for the payments made on the loan(s).

17. Documentation that shows the spot rates for all the foreign currency option pairs transacted for each day from the Trade Date until the Expiration Date.

18. Documentation that shows how the Market Value was determined for any foreign currency sold by the investor(s) or any of the entities that participated in the transaction.

19. If any document is withheld on the grounds of privilege, state, with respect to each document withheld:

a. Name and title of the document author;
b. Date of the document;
c. Names, titles and addresses of all recipients of the documents and/or copies thereof;
d. Subject matter of the documents;
e. Privilege of protection claimed;
f. Number of the request to which the production of the documents would otherwise be responsive.

Foreign Currency Digital Option Investor Questions

1. Please describe when and how you first came to know about the currency digital option transaction. Include the names of all individuals and firms who introduced you to this transaction.

2. Please describe the representations made to you by any individual pertaining to the digital option transaction. Include in your description, a description of the written materials you received or were able to view to help you understand the transaction and its benefits.

3. Provide the names and firms of all individuals who either presented this information to you or were present when the information was presented.

4. Provide the dates and a brief description of all presentations made to you regarding this transaction. (Ex: meetings, slide shows, flowcharts, models, etc.)

[12]

5. Were you allowed to keep all written material provided to you with regard to this transaction? If not, why were you not allowed to keep the materials?

6. Were any other strategies presented to you in addition to the currency digital option strategy? If so, please describe the strategy, who presented it to you, what materials you may have pertaining to the strategy, and why you did not enter into the strategy.

7. Please explain your understanding of how a currency digital option operates.

8. What is your previous experience with regard to currency digital option investing or trading?

9. What type of research did you conduct with regard to understanding this type of option strategy?

10. If you had no previous experience and/or no specific knowledge of this type of option investing or trading, why did you enter into the transaction?

11. What was your understanding of the benefit of using a currency digital option?

12. What was your understanding of how this benefit differs from another form of option, for example, how does it differ from a standard, plain vanilla option on foreign currency?

13. Were you told upfront (or at any time during the transaction) that you would have to form other entities (partnership, LLC, S Corp, Trust) in order to implement this transaction?

a. Who told you this?
b. What were you told regarding the purpose of forming the other entities rather than you personally entering into the long and short option positions yourself?
c. Did you form the entity(ies) or did someone do it for you? Who?

14. Were you told upfront (or at any time during the transaction) that one of the entities would transfer or assign the open option positions (long and short) to another related entity such?

a. Who told you this?
b. What were you told regarding the purpose of forming the other entity?
c. Did you form the entity(ies) or did someone do it for you? Who?

15. Were you told upfront (or at anytime during the transaction) that the other entity would let the options expire unexercised?

a. Who told you this?
b. What were you told regarding the expiration of the options?

[13]

16. Were you told upfront (or at anytime during the transaction) that the other entity would be terminated shortly after the maturity date of the options?

a. Who told you this?
b. What do you recall being told about this termination?

17. Were you told upfront (or at anytime during the transaction) that this was only a 30-day investment strategy?

    a. Who told you this?
    b. What do you recall being told about this termination?

18. Were you told upfront (or at anytime during the transaction) that there would be a purchase and liquidating distribution of foreign currency as part of this transaction?

    a. Who told you this?
    b. What do you recall being told about this distribution?

19. Identify the party who purchased the foreign currency from you after the distribution. Were you personally involved in this phase of the transaction? If not, who did it for you?

20. Were you told upfront (or at anytime during the transaction) that the digital options were structured in such a way that there would not be a risk of significant gain or loss on the transaction?

    a. Who told you this?
    b. What do you recall being told about this?

21. Did you at any time feel that your initial investment was at-risk? Please explain your feelings or thoughts on your risk potential.

22. Were you told upfront (or at anytime during the transaction) that in the end you would receive your original investment back less the appropriate fees?

a. Who told you this?
b. What do you recall being told about this?

23. Were you told upfront (or at anytime during the transaction) that the benefit of this currency digital option transaction was based on an interpretation of the tax laws?

a. Who told you this?
b. What do you recall being told about this?

24. Did you receive a tax opinion on this currency digital option strategy?

a. Who authored the opinion?
[14]
b. How much did you pay for the opinion?
c. Provide a copy of the opinion.

25. Were you told upfront (or at anytime during the transaction) that your additional upfront investment in the entity (partnership, S-Corp, or LLC) would be 2% of your desired loss?

a. Who told you this?
b. What do you recall being told about this?

26. Did you enter into this transaction because you desired to create a loss for federal income tax purposes? If not, please explain why the necessary additional upfront investment correlation with 2% of a "desired loss"?

27. How were the payout amounts in your contract determined?

28. Who made this determination? (I.E., Party A? Party B? Someone else?)

29. How were the settlement dates in your contracts determined?

30. Who made this determination? (I.E., Party A? Party B? Someone else?)

31. How were the maturity dates in your contracts determined?

32. Who made this determination? (I.E., Party A? Party B? Someone else?)

33. What reference, device, etc. was used to obtain the spot rate at the maturity date? (I.E., on the maturity date, what does the calculation agent refer to in order to obtain the spot rate?)

34. Were you able to monitor the daily spot rates during the term of your contracts to see how you were doing? If so, what service or other published source did you use?

35. Where is the profit potential in the transactions where both Party A and Party B take the same directional movement on the spot? (I.E., if both will "win" or "lose" if the spot rate at maturity is equal to or greater than the strike price, how can a profit greater than the net difference between the long and short positions be achieved).

36. When both Party A and Party B take the same directional movement on the spot rate, does this not limit the risk involved?

37. How can we verify that your over-the-counter option transactions took place?

38. Do you know if these transactions go through a Clearing House? If yes, please identify the Clearing House(s) used.

39. If the transactions did not go through a Clearing House, please explain.

[15]

40. Do you know which agency regulates these contracts?

41. Did you actually pay the premium amount stated in the contracts? (I.E., was there a physical transfer of funds or was there a net settlement?)

42. Did you actually receive from the counterparty the premium amount stated in the contracts? (I.E., was there a physical transfer of funds or was there a net settlement?)

43. If there was an actual payout, or a net settlement payout, how many days after the date the contract was entered into did the physical payment take place? How was this done (I.E., were physical funds transferred to/from you? If not, explain)

44. Did the net settlement on the premiums represent a fee to any party? If so, which party?

45. Were you provided any other documents other than the confirmation statements as evidence of the transaction? If so, describe and provide copies.

46. Describe the documents you were required to sign in order to enter into the contracts. Were you provided copies? If so, describe and provide copies.

47. Were you required to maintain a margin account or any other similar account with the counterparty? If so, please describe. If not, how did you secure the transaction?

48. Were you provided the name(s) of a contact person at Counterparty whom you could call? If so, provide the name(s), title(s), address(es), and telephone number(s).

49. If not, who could you call/speak to if you had questions or concerns pertaining to the transaction? Provide name(s), title(s), address(es), and telephone number(s).

50. Were you provided the name(s) of a contact person at [Accounting and/or Law Firm] whom you could call? If so, provide the name(s), title(s), address(es), and telephone number(s).

51. What fees did you pay to enter into these contracts (outside of the premium amounts)? Describe fee type, amount, date paid and to whom paid. Provide copies of checks (front and back)

52. Did you pay legal fees, accounting fees, brokerage fees, or any other fees related to this transaction? Describe fee type, amount, date paid and to whom paid. Provide copies of checks (front and back)

[16] **Foreign Currency Digital Option Promoter Questions**

1. Please describe when and how you first came to know about the foreign currency digital option transaction. Include the names of all individuals and firms who introduced you to this transaction

or who assisted you in developing this transaction.

2. Please describe the representations you made to potential customers regarding the foreign currency digital option transaction. Include in your description, a description of the written materials you used in presenting this transaction to potential customers to help them understand the transaction and its benefits.

3. Did you allow potential customers to keep all written materials they were provided with regard to this transaction? If not, describe the materials they were allowed to view but not keep and explain why they were not allowed to keep the materials.

4. Provide the names and firms of all individuals who either presented this information with you or were present when you presented this information to potential clients.

5. Provide the dates and a brief description of all presentations you made to potential customers regarding this transaction (e.g. meetings, slides shows, flowcharts, models, etc.).

6. In addition to the foreign currency digital option strategy, did you present any other strategies to these potential customers for their consideration? If so, please describe the other strategy(ies), who presented the strategy(ies), and why the customer chose to enter into the digital option strategy instead of the other strategy(ies).

7. Did you or any of your assistants maintain a file(s) on each customer who was presented this

foreign currency digital option transaction and/or who entered into this foreign currency digital option transaction? If so, describe the information that is contained in the files; how the files are coded within your organization with respect to each customer; and where the files are located at this time.

8. Please explain your understanding of how a foreign currency digital option operates.

9. What is your previous experience with regard to foreign currency digital option investing or trading?

10. What type of research did you conduct with regard to understanding this type of option strategy?

11. If you had no previous experience and/or no specific knowledge of this type of option investing or trading, why did you recommend this transaction to potential customers?

12. What was your understanding of the benefit of using a foreign currency digital option?

[17]

13. What was your understanding of how this benefit differs from another form of option, for example, how does it differ from a standard, plain vanilla option on foreign currency?

14. Were potential customers told upfront (or at any time during the transaction) that they would have to form other entities (partnership, LLC, Sub-S corporation, trust) in order to implement this transaction?

a. Who told the potential customer this?
b. What were potential customers told regarding the purpose of forming the other entities rather than personally entering into the long and short option positions themselves?
c. Did you form the entities for the customers or did someone else do it? Who?

15. Were potential customers told upfront (or at any time during the transaction) that one of the entities would transfer or assign the open option positions (long and short) to another related entity?

a. Who told the potential customers this?
b. What were potential customers told regarding the purpose of transferring or assigning the open option positions to another related entity?
c. Did you form the related entity(ies) for the customers or did someone else do it? Who?

16. Were potential customers told upfront (or at anytime during the transaction) that the other entity would let the option expire unexercised?

a. Who told the potential customers this?
b. What were the potential customers told regarding the expiration of the options?

17. Were potential customers told upfront (or at anytime during the transaction) that the other entity would be terminated shortly after the maturity date of the options?

a. Who told the potential customers this?
b. What were the potential customers told regarding the termination of the entity shortly after the options matured?

18. Were potential customers told upfront (or at anytime during the transaction) that this was only a short-term and/or one-time investment strategy?

    a. Who told the potential customers this?
    b. What were the potential customers told about the duration of this strategy?

19. Were potential customers told upfront (or at any time during the transaction) that there would be a purchase and liquidating distribution of foreign currency as part of this transaction?

    a. Who told the potential customers this?
    [18]

    b. What were the potential customers told about the purpose of the purchase and distribution of the foreign currency with respect to this transaction?

20. Identify the party or parties who purchased the foreign currency from the customers after the distribution. Were you personally involved in this phase of the transaction? If not, who handled it for the customer?

21. Were potential customers told upfront (or at anytime during the transaction) that the foreign currency digital options were structured in such a way that there would not be a risk of significant gain or loss on the transaction?

    a. Who told the potential customers this?
    b. What were the potential customers told about their risk of significant gain or loss on the transaction?

22. Were potential customers told upfront (or at anytime during the transaction) that in the end they would receive their original investment back less the appropriate fees?

    a. Who told the potential customers this?
    b. What were the potential customers told regarding the net return of their initial investment?

23. Were potential customers told upfront (or at anytime during the transaction) that the benefit of this foreign currency digital option transaction was based on an interpretation of the tax laws?

    a. Who told the potential customers this?
    b. What were the potential customers told regarding the interpretation of the tax laws with respect to this transaction?

24. Were potential customers told upfront (or at anytime during the transaction) that the additional upfront investment in the entity (partnership, Sub-S corporation, or LLC) would be 2% of the desired tax loss?

    a. Who told the potential customers this?
    b. What were the potential customers told regarding the amount of upfront investment in relation to the amount of the desired tax loss?

25. Did potential customers enter into this transaction because they desired to create a loss for federal income tax purposes? If not, please explain why the necessary additional upfront investment correlates with 2% of a "desired loss."

26. How were the payout amounts in the option contracts determined?

27. Who made this determination? (i.e.: Party A? Party B? If someone else, who?)

[19]

28. How were the settlement dates in the option contracts determined?

29. Who made this determination? (i.e.: Party A? Party B? If someone else, who?)

30. How were the maturity dates in the option contracts determined?

31. Who made this determination? (i.e.: Party A? Party B? If someone else, who?)

32. What reference, devices, etc. was used to obtain the spot rate at the maturity date? (i.e.: on the maturity date, what does the calculation agent refer to in order to obtain the spot rate?)

33. When both Party A and Party B take the same directional movement on the spot rate, does this not limit the risk involved?

34. Were you aware that the only meaningful profit potential on the transaction existed in the scenario whereby the spot price fell within the "spread" and that the transaction was structured so that this would never actually occur since the Counterparty could, under the terms of the contract, disregard any spot rate it determined not to be "commercially reasonable?" Were potential customers made aware of this lack of any significant profit potential?

35. How can we verify that these over the counter option transactions actually took place?

36. Do you know if these transactions go through a clearing house? If yes, please identify the clearing house(s) used.

37. If the transactions did not go through a clearing house, please explain.

38. Do you know which agency regulates these contracts? If so, please provide the name(s) of the agency.

39. Did the net settlement on the premiums represent a fee to any party? If so, which party?

40. Did you provide the customers with any documents other than the confirmation statements as evidence of the transaction? If so, please describe. If not, how did the counterparty secure the transaction?

41. Were the customers required to maintain a margin account or any other similar account with the counterparty? If so, please describe. If not, how did the counterparty secure the transaction?

42. What documents, financial information, etc. were the customers required to provide to the counterparty in order to do business with them with respect to this transaction?

43. Were the customers provided the name(s) of a contact person at the counterparty whom they could call? If so, provide the name(s), title(s), address(es), and telephone [20] number(s).

44. If not, who could the customers call or speak to if they had questions or concerns pertaining to the transaction? Provide name(s), title(s), address(es), and telephone number(s).

45. Describe all the fees that were paid by the customer with respect to this foreign currency digital option strategy. (Describe the fee type, amount, and to whom paid.)

LMSB & SB/SE Tracking Codes; UIL Codes

Both the Financial Products Specialist and the Revenue Agent need to make sure that the tax shelter case is properly reported on ERCS/CEMIS. The Office of Tax Shelter Analysis has published the following information with respect to tracking and UIL codes for the Son of BOSS transaction. Check the LMSB OTSA website for updates and coding for other tax shelters.

LMSB & SB/SE Tracking Code: **9767**
Uniform Issue List: **9300.13-00**

Internal Revenue Service Position

At the time of this writing, the Service has not issued an official position paper with respect to the specific variations of the SOB Transaction. However, several reports are pending in Counsel with respect to transactions in which the short sale of Treasury Notes is involved. In it, the Service is relying in part to disallow the claimed loss based on Rev. Rul. 95-26, 1995-1 CB 131 and *Salina Partnership, LP, FPL Group, Inc. v. Comm'r., T. C. Memo 2000-352, 80 T.C.M. 686*.

These cases state that the open position is an obligation for purposes of IRC §752 and must be accounted for in the outside basis of partnership interest.

Reports are also pending in Counsel with respect to positions disallowing the loss on digital option transactions. These cases do not use the Salina arguments stated above.

Expenses related to the transaction are addressed in *Nicole Rose Corp. v. Comm'r., 117 T.C. 328 (2001), aff'd, 320 F. 3d 282, 2003-1 U.S.T.C. ¶50,137 (2002)*.

[21] CB-NOTICE, 2000FED ¶46,508. **Loss deductions, disallowance of: Artificial losses: Abusive tax shelters: Partnerships: Basis.** –, Cumulative Bulletin Notice 2000-44 I.R.B. 2000-36, (Aug. 11, 2000)----------

Cumulative Bulletin Notice 2000-44, , August 11, 2000. 2000-36 I.R.B.

[*Code Secs. 165, 183 and 701*]

Loss deductions, disallowance of: Artificial losses: Abusive tax shelters: Partnerships: Basis. – Certain transactions that are being marketed for the purpose of generating tax losses will not produce deductible losses for federal income tax purposes. These arrangements purport to give taxpayers an artificially high basis in their partnership interests and, thereby, give rise to deductible losses on the disposition of those partnership interests, even though the taxpayers experienced no corresponding economic

losses. BACK REFERENCES: ¶9804.01, 12,177.055 and 25,062.077.

[*Code Secs. 6011, 6111, 6112, 6662, 6694, 6700, 6701, 6707 and 6708*]

Penalties, civil: Negligence: Abusive tax shelter: Reliance on promoter: Return preparer: Aiding or abetting: Failure to provide tax shelter information: Tax returns: Tax shelter reporting: Reportable transactions: Listed transactions: Registration of tax shelters: Lists of investors. – Certain transactions that are being marketed for the purpose of generating tax losses, with no corresponding economic losses, by purporting to give taxpayers an artificially high basis in their partnership interests have been identified as "listed transactions" that may be subject to the tax shelter registration and list maintenance requirements. In addition, penalties may be imposed on participants in these transactions or, if applicable, on persons who participate in the promotion or reporting of these transactions. BACK REFERENCES: ¶35,141.06, 37,002.01, 37,022.01, 39,651G.81, 39,960.01, 40,030.41, 40,035.01, 40,090.20 and 40,100.01.

In Notice 99-59, 1999-52 I.R.B. 761, the Internal Revenue Service and the Treasury Department described certain transactions that were being marketed to taxpayers for the purpose of generating artificial tax losses. This notice concerns other similar transactions that purport to generate tax losses for taxpayers.

As stated in Notice 99-59, a loss is allowable as a deduction for federal income tax purposes only if it is bona fide and reflects actual economic consequences. An artificial loss lacking economic substance is not allowable. See *ACM Partnership v. Commissioner*, 157 F.3d 231, 252 (3d Cir. 1998), *cert. denied*, 526 U.S. 1017 (1999) ("Tax losses such as these . . . which do not correspond to any actual economic losses, do not constitute the type of 'bona fide' losses that are deductible under the Internal Revenue Code and regulations."); *Scully v. United States*, 840 F.2d 478, 486 (7th Cir. 1988) (to be deductible, a loss must be a "genuine economic loss"); *Shoenberg v. Commissioner*, 77 F.2d 446, 448 (8th Cir. 1935) (to be deductible, a loss must be "actual and real"); §1.165-1(b) of the Income Tax Regulations ("Only a bona fide loss is allowable. Substance and not mere form shall govern in determining a deductible loss.").

[22] Notice 99-59 describes an arrangement that purported to give rise to deductible losses on disposition of stock by applying the rules relating to distributions of encumbered property to shareholders in order to create artificially high basis in the stock. The Service and the Treasury have become aware of similar arrangements that have been designed to produce noneconomic tax losses on the disposition of partnership interests. These arrangements purport to give taxpayers artificially high basis in partnership interests and thereby give rise to deductible losses on disposition of those partnership interests.

One variation involves a taxpayer's borrowing at a premium and a partnership's subsequent assumption of that indebtedness. As an example of this variation, a taxpayer may receive $3,000X in cash from a lender under a loan agreement that provides for an inflated stated rate of interest and a stated principal amount of only $2,000X. The taxpayer contributes the $3,000X to a partnership, and the partnership assumes the indebtedness. The partnership thereafter engages in investment activities. At a later time, the taxpayer sells the partnership interest.

Under the position advanced by the promoters of this arrangement, the taxpayer claims that only the stated principal amount of the indebtedness, $2,000X in this example, is considered a liability assumed by the partnership that is treated as a distribution of money to the taxpayer that reduces the basis of the taxpayer's partnership interest under §752 of the Internal Revenue Code. Therefore, disregarding any additional amounts the taxpayer may contribute to the partnership, transaction costs, and any income realized or expenses incurred at the partnership level, the taxpayer purports to have a basis in the partnership interest equal to the excess of the cash contributed over the stated principal amount of the indebtedness, even though the taxpayer's net economic outlay to acquire the partnership interest and the value of the partnership interest are nominal or zero. In this example, the taxpayer purports to have a basis in the partnership interest of $1,000X (the excess of the cash contributed ($3,000X) over the stated principal

amount of the indebtedness ($2,000X)). On disposition of the partnership interest, the taxpayer claims a tax loss with respect to that basis amount, even though the taxpayer has incurred no corresponding economic loss.

In another variation, a taxpayer purchases and writes options and purports to create substantial positive basis in a partnership interest by transferring those option positions to a partnership. For example, a taxpayer might purchase call options for a cost of $1,000X and simultaneously write offsetting call options, with a slightly higher strike price but the same expiration date, for a premium of slightly less than $1,000X. Those option positions are then transferred to a partnership which, using additional amounts contributed to the partnership, may engage in investment activities.

Under the position advanced by the promoters of this arrangement, the taxpayer claims that the basis in the taxpayer's partnership interest is increased by the cost of the purchased call options but is not reduced under §752 as a result of the partnership's assumption of the taxpayer's obligation with respect to the written call options. Therefore, disregarding additional amounts contributed to the partnership, transaction costs, and any income realized and expenses incurred at the partnership level, the taxpayer purports to have a basis in the partnership interest equal to the cost of the purchased call options ($1,000X in this example), even though the taxpayer's net economic outlay to acquire the partnership inter-

est and the value of the partnership interest are nominal or zero. On the disposition of the partnership interest, the taxpayer claims a tax loss ($1,000X in this example), even though the taxpayer has incurred no corresponding economic loss.

[23] The purported losses resulting from the transactions described above do not represent bona fide losses reflecting actual economic consequences as required for purposes of §165. The purported losses from these transactions (and from any similar arrangements designed to produce noneconomic tax losses by artificially overstating basis in partnership interests) are not allowable as deductions for federal income tax purposes. The purported tax benefits from these transactions may also be subject to disallowance under other provisions of the Code and regulations. In particular, the transactions may be subject to challenge under §752, or under §1.701-2 or other anti-abuse rules. In addition, in the case of individuals, these transactions may be subject to challenge under §165(c)(2). See *Fox v. Commissioner*, 82 T.C. 1001 (1984). Furthermore, tax losses from similar transactions designed to produce noneconomic tax losses by artificially overstating basis in corporate stock or other property are not allowable as deductions for federal income tax purposes.

Appropriate penalties may be imposed on participants in these transactions or, as applicable, on persons who participate in the promotion or reporting of these transactions, including the accuracy-related penalty under §6662, the return preparer penalty un-

der §6694, the promoter penalty under §6700, and the aiding and abetting penalty under §6701.

Transactions that are the same as or substantially similar to the transactions described in this Notice 2000-44 are identified as "listed transactions" for the purposes of §1.6011-4T(b)(2) of the Temporary Income Tax Regulations and §301.6111-2T(b)(2) of the Temporary Procedure and Administration Regulations. See also §301.6112-1T, A-4. It should be noted that, independent of their classification as "listed transactions" for purposes of §§1.6011-4T(b)(2) and 301.6111-2T(b)(2), the transactions described in this Notice 2000-44 may already be subject to the tax shelter registration and list maintenance requirements of §§6111 and 6112 under the regulations issued in February 2000 (§§301.6111-2T and 301.6112-1T, A-4), as well as the regulations issued in 1984 and amended in 1986 (§§301.6111-1T and 301.6112-1T, A-3). Persons required to register these tax shelters who have failed to register the shelters may be subject to the penalty under §6707(a) and to the penalty under §6708(a) if the requirements of §6112 are not satisfied.

In addition, the Service and the Treasury have learned that certain persons who have promoted participation in transactions described in this notice have encouraged individual taxpayers to participate in such transactions in a manner designed to avoid the reporting of large capital gains from unrelated transactions on their individual income tax returns (Form 1040). Certain promoters have recommended that

taxpayers participate in these transactions through grantor trusts and use the same grantor trusts as vehicles to realize the capital gains. Further, although each separate capital gain and loss attributable to a portion of a trust that is treated as owned by a grantor under the grantor trust provisions of the Code (§671 and following) is properly reported as a separate item on the grantor's individual income tax return (see §1.671-2(c) and the Instructions to Form 1041, U.S. Income Tax Return for Estates and Trusts), the Service and the Treasury understand that these promoters have advised that the capital gains and losses from these transactions may be netted, so that only a small net capital gain or loss is reported on the taxpayer's individual income tax return. In addition to other penalties, any person who willfully conceals the amount of capital gains and losses in this manner, or who willfully counsels or advises such concealment, may be guilty of a criminal offense under §§7201, 7203, 7206, or 7212(a) or other provisions of federal law.

The principal authors of this notice are David A. Shulman of the Office of Associate Chief Counsel [24] (Passthroughs and Special Industries) and Victoria S. Balacek of the Office of Associate Chief Counsel (Financial Instruments and Products). For further information regarding this notice, contact Mr. Shulman at (202) 622-3080 or Ms. Balacek at (202) 622-3930 (not toll free calls).